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ABSTRACT

This instructional guide was designed to assist educators in teaching the topics of consumer credit and consumer credit protection to secondary and postsecondary students in various economics and business courses, as well as for use in adult and community education courses. The guide contains four sections, which can be used singly or in combination. They cover: (1) an overview of consumer credit; (2) the Equal Credit Opportunity Act; (3) the Fair Credit Reporting Act; and (4) the Fair Debt Collection Practices Act. Through the study of these laws and topics, students learn about types of consumer credit, the pros and cons of credit use, creditworthiness, credit reporting, consumer delinquency, credit shopping, and billing errors. Each of the sections contains five or six individual topics focusing on specific concepts or skills. These units are sequentially organized with the earlier topics presenting basic concepts and skills that provide the necessary background for the subsequent topics. In addition to directions, each section contains an introduction, key concepts and definitions of terms, an answer key, and information sheets which may serve as masters for overhead transparencies or instructional materials for students. A pretest is also included with each section to help instructors assess student knowledge and select appropriate sections and topics. The guide notes that two additional sections, truth in lending and the Fair Credit Billing Act, will be available at a later date. (AYC)

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An Instructional Unit on Consumer Credit Protection

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May 1982

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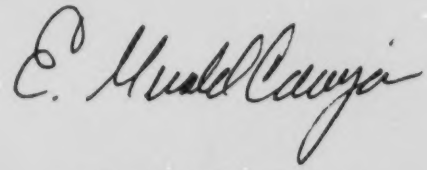
Forward

We at the Federal Reserve Bank of Minneapolis believe it is important for consumers to know how to establish and use credit responsibly—it is important for them as individuals and it is important for the economy at large. Consumers should also be aware of protection provided to them by the consumer credit protection laws enacted by Congress since 1968. We are pleased to introduce *Your Credit Rights.* This publication is designed to provide a structure for teaching the topics of consumer credit and consumer protection.

The unit has been developed in conjunction with educators as well as representatives of the credit industry. We hope teachers, future credit users, and consumers who now use credit will find *Your Credit Rights* to be an effective educational tool.



E. Gerald Corrigan, President
Federal Reserve Bank
of Minneapolis

Acknowledgments

Your Credit Rights was developed by the Federal Reserve Bank of Minneapolis. It is the result of cooperative efforts of Jean A. Kinsey, Associate Professor, Agricultural and Applied Economics Department, University of Minnesota; Judith A. Remington, Attorney-at-Law and consultant to the Bank; and Barbara J. Bergerson of the Bank's Public Information staff who served as project leader for *Your Credit Rights.*

We especially wish to thank the Ninth Federal Reserve District educators who encouraged us to undertake this project and assisted us during the development and classroom testing of *Your Credit Rights.* It is our hope that this unit will serve as a valuable resource in the teaching of consumer credit concepts and skills.

We also thank the individuals and organizations representing the credit industry whose assistance proved invaluable in the development of these materials.

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Preface

Unit's Purpose

Your Credit Rights was developed by the Federal Reserve Bank of Minneapolis to assist educators in teaching the topics of consumer credit and consumer credit protection. It is designed for use with secondary and post-secondary students in economics, consumer economics, business education, home economics, or law-related courses, as well as in adult and community education programs on consumer credit.

The purpose of the unit is threefold:

1. To increase student awareness of the role played by individuals, creditors, credit bureaus, and debt collectors in the credit process.
2. To increase student understanding of the legal rights and responsibilities of consumers, creditors, and other representatives of the credit industry.
3. To help consumers develop skills in establishing and using consumer credit and solving credit-related problems.

Content and Organization

Your Credit Rights contains six separate sections which can be used singly or in conjunction with the other sections in the unit. Sections included are:

Section 1—An Overview of Consumer Credit
Section 2—The Equal Credit Opportunity Act
Section 3—The Fair Credit Reporting Act
Section 4—The Fair Debt Collection Practices Act
*Section 5—Truth in Lending
*Section 6—The Fair Credit Billing Act

The unit is designed so instructors can teach one or more sections, depending on the time available and the needs of their students. Section 1 provides an overview of consumer credit and explores the individual's use of credit. Although it provides a good foundation for studying the individual credit protection laws, all sections are self-contained and do not depend on the use of specific activities from a previous section to meet their instructional objectives. A pretest provided for each section of *Your Credit Rights* may be used to assess student knowledge and help an instructor select appropriate sections and topics to teach.

Each section of *Your Credit Rights* contains individual topics focusing on specific concepts or skills. Several learning activities

*Available at a later date

and a variety of teaching strategies are used to meet the topic's instructional objective. Instructors may select topics and activities within a section that are most appropriate for use with their students and their individual teaching styles.

Sections are developed sequentially. Earlier topics present basic information, concepts, and skills that provide students with the necessary background to study the topics and concepts that follow. For example, in Section 1, students first learn about the types of consumer credit and reasons why people use credit. Later they study the pros and cons of credit use and the factors to consider when deciding how to make a purchase. Similarly, in Sections 2-6, students learn about creditworthiness, credit reporting, consumer delinquency, credit shopping, and billing errors as a basis for studying the specific consumer credit protection laws.

Using *Your Credit Rights*

Each topic is designed to be taught during a class period of 40-55 minutes. If individual class periods are shorter, an instructor may wish to limit the number of activities used to teach a topic or use more than one class period. Additional class time also may be needed to develop, conduct, or follow up on role play and simulation activities. Five or six topics are covered in each section. Therefore, a section may be taught during a one- or two-week period, depending on the use of role play and simulation activities, the amount of class time available, the level and background of students, the number of topics and activities used, and the use of additional materials.

Prior to teaching a topic, an instructor should carefully review the learning objective for the topic, the list of materials needed, and topic directions printed on the instructional folder for each section. In addition, transparencies, readings, student exercises, case studies, flow charts, etc., contain information that an instructor may wish to review before using these materials in class. Although topic directions and student materials are designed to provide the instructor with all the information needed to teach a topic, role play and simulation activities may require some additional preparation such as a test run.

All materials needed to teach *Your Credit Rights* are included in the instructional package. Instructors may find the *Introduction to Your Credit Rights* helpful in explaining to students the legislative and enforcement aspects of consumer credit protection. Besides topic directions, each instructional folder contains an introduction to the section, key concepts and definitions of key terms used in the section, and an answer key. The individual sheets following each section folder are "masters" which an instructor may use to make overhead transparencies and classroom sets of student materials needed to teach each topic.

All materials are three-hole punched so that an instructor may place *Your Credit Rights* in a three-ring binder and remove individual folders or sheets for lesson preparation and classroom use. This will also facilitate the adding of future sections and the updating of materials by the Federal Reserve Bank of Minneapolis when consumer credit laws and regulations change. If you wish to have your name placed on a mailing list to receive updates to *Your Credit Rights*, as well as additional sections when they are available, please return the enclosed post card. If your mailing address changes, please notify us by writing the Federal Reserve Bank of Minneapolis, Office of Public Information, 250 Marquette Avenue, Minneapolis, MN 55480, or call us at (612) 340-2443.

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Introduction

The era of consumer credit protection began with two very simple ideas—that the consumer should know more about the costs of credit and that all consumers should be treated fairly. These two ideas have led to hundreds of pages of laws, regulations, and interpretations.

Your Credit Rights: An Instructional Unit on Consumer Credit Protection attempts to take this complex area of law and economics and provide information which all users of credit need to make informed credit decisions. Excerpts from testimony before House and Senate hearings, case studies, and role play and simulation activities are used to stimulate interest in the topic of consumer credit protection and the specific credit laws. Also, they provide students an opportunity to apply knowledge and skills they have learned about obtaining and using credit and solving credit-related problems. Readings, graphic illustrations, overheads, flow charts, student exercises, and other approaches have also been used to vary the format.

Your Credit Rights deals only with consumer credit, not business or agricultural credit. Consumer credit is generally defined as credit used for personal and household needs. This includes financing a car, furniture, or appliances and open-end financing, such as a credit line in conjunction with a transaction account, a bank credit card, or a department store credit account. Although the use of credit to finance a real estate transaction is also considered consumer credit, these materials do not cover mortgage credit.

The passage of individual consumer credit protection legislation is only the first step in developing practical "rules" for consumers, creditors, and other representatives of the credit industry to follow. The overall regulation process involves five essential steps which are described below.

Legislation

The ideas for legislation come from many sources—magazines, newspapers, letters from constituents, etc. For example, the Fair Credit Reporting Act began as a single letter from a constituent to Senator William Proxmire. Wherever the initial idea comes from, a senator or representative introduces legislation, and extensive hearings are held on the proposed bill. If a bill is passed by the Congressional subcommittees and committees, it is voted on by the House and Senate. If passed, it goes to the President for his signature or veto.

Regulation

A federal agency, most often the Federal Reserve System, is designated to issue a "regulation" to provide specific rules to implement the provisions of the law. The agency proposes a regulation and consumers, creditors and others in the credit industry, and legislators have an opportunity to comment on whether the regulation is fair and meets the purposes for which it is intended. Often, the regulation will go through several drafts before it is final. Regulations are often amended after they are adopted.

Interpretation

Inevitably, the regulation does not answer every question. A creditor or a consumer will write the Federal Reserve System, for example, and ask how the regulation applies to a particular situation. The Board of Governors of the Federal Reserve System or their staff may then issue an interpretation. This interpretation will help resolve the situation in question, and it is often used to resolve future similar situations.

Enforcement

Examiners from the Federal Reserve System and other agencies regularly examine banks, credit unions, savings and loan associations, etc., to see that they comply with the consumer credit protection laws. These examinations often serve to educate creditors and to identify problem areas in the regulations. If repeated violations are found, the agency may take enforcement action against a particular creditor. Also, all agencies given authority to enforce these laws investigate consumer complaints.

Litigation

The courts inevitably decide how a particular law will be interpreted. For example, a consumer may sue a creditor for violation of the law. The court will decide whether or not the creditor is at fault. And, if a violation is found, the court will decide which remedies are appropriate. Or, a creditor may sue the enforcement agency, arguing that its actions go beyond its authority. Again, the courts will determine whether the enforcement agency has acted within its jurisdiction.

While it is helpful to break the regulation process down into these five areas, it is important to remember that there is often activity in all these areas simultaneously. For example, while Congress was amending Truth in Lending to simplify it, the Federal Reserve System was proposing its own changes in the regulation. And interpretation, enforcement, and litigation continued unaffected by the work in Congress. Therefore, consumer credit is a difficult area to teach, not only because of its complexity, but because it is ever-changing.

The following chart lists consumer credit protection legislation in the order it was enacted. It is intended for your reference throughout the unit.

	Passed	Amended	Effective Date	Purpose
Truth in Lending	1968	1976	1969	To give the consumer information on credit costs before he/she enters into a credit transaction and to encourage credit shopping.
Fair Credit Reporting Act	1969	None	1970	To allow the consumer to learn of and challenge information about himself/herself contained in credit reports.
Equal Credit Opportunity Act*	1974	1976	1975	To prohibit credit denial based on sex, marital status, age, race, religion, national origin, receipt of public assistance, or good faith exercise of consumer credit protection rights.
Fair Credit Billing Act	1974	None	1975	To allow the consumer to effectively resolve billing disputes with credit card companies and other open-end creditors.
Fair Debt Collection Practices Act	1977	None	1978	To protect the consumer from abusive debt collection practices and allow the consumer to obtain verification of a debt.
Truth in Lending Simplification Act	1980	None	1982	To simplify Truth in Lending forms and procedures to make them more usable by the consumer.

*An earlier act, the Fair Housing Act of 1968, prohibits discrimination by race, color, religion, sex, or national origin in lending for purchase or improvement of a home.

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Consumer Credit Information from the Federal Reserve System

The following materials are designed for use with secondary and post-secondary students as well as adults and community groups. Except where noted, materials are available free of charge from the publishing Federal Reserve Bank or the Board of Governors of the Federal Reserve System. Addresses are provided at the end of the listing.

Publications

The ABC's of Figuring Interest
Discusses how the various ways of calculating interest affect the dollar amount paid. Federal Reserve Bank of Chicago, 1979, 10 pp.

Alice in Debitland
Explains consumer protection under the Electronic Fund Transfer Act, including the use of debit cards. Board of Governors of the Federal Reserve System, 1980, 16 pp.

The Arithmetic of Interest Rates
Applies the concepts of simple and compound interest to practical problems of determining the yield on government securities and the cost of consumer credit. Federal Reserve Bank of New York, 1981, 36 pp.

Fedpoints 17—Consumer Credit Regulators
Reviews the responsibilities of the 12 federal organizations charged with administering consumer regulations. Federal Reserve Bank of New York, 1981, 4 pp.

Consumer Credit Terminology Handbook
Defines consumer credit terms to assist consumers in everyday credit transactions. Also available in Spanish. Federal Reserve Bank of New York, 1980, 20 pp.

Consumer Education Catalog
Lists consumer education materials published by the System. Federal Reserve Bank of Boston, 1980, 24 pp.

Consumer Handbook to Credit Protection Laws
Explains how consumer credit laws can help in shopping for credit, applying for credit, and establishing a good credit record. Board of Governors of the Federal Reserve System, 1981, 56 pp.

Credit Guide
Provides information to help consumers get a good start, avoid hazards, and know what to do and where to go if they have problems using credit. Federal Reserve Bank of Chicago, available June 1982.

Credit Points
Discusses the major credit laws such as Truth in Lending and describes consumers' rights and protections. Federal Reserve Bank of Boston, rev. 1980, 24 pp.

Give Yourself Credit
Guides the consumer through various credit protection laws. Federal Reserve Bank of San Francisco, 1981, 40 pp.

The Story of Consumer Credit
Explains credit rights and responsibilities and introduces consumer credit regulations in a cartoon format. Also available in Spanish. Federal Reserve Bank of New York, 1980, 24 pp. (Charges for some bulk orders)

Pamphlets

Board of Governors of the Federal Reserve System:

The Equal Credit Opportunity Act and Age, 1977
The Equal Credit Opportunity Act and Credit Rights in Housing, 1980
The Equal Credit Opportunity Act and Incidental Creditors, 1977
The Equal Credit Opportunity Act and Women, 1977
Fair Credit Billing, 1976
How to File a Consumer Credit Complaint, 1978
If You Borrow to Buy Stock, 1972
If You Use a Credit Card, 1978
What Truth in Leasing Means to You, 1978
What Truth in Lending Means to You, 1981

Federal Reserve Bank of Cleveland:

The Flip Side of Credit, 1981

Federal Reserve Bank of New York:

Credit-Ability, 1980
On Using Credit, 1980
Your Credit Rating, 1979

Federal Reserve Bank of Philadelphia:

Electronic Fund Transfer (Regulation E), 1980
The Fair Debt Collection Practices Act, 1978
How the New Equal Credit Opportunity Act Affects You, 1977
How to Establish and Use Credit, 1976
Options for Savers, 1980
The Rule of 78's, 1978
Your Credit Rating, 1979

Instructional Materials

Credit-Scope
Outlines basic credit concepts in a learning kit consisting of a

poster, 12 lesson plans, and a teacher's curriculum guide. Federal Reserve Bank of New York, 1980. (Secondary instructors)

Equal Credit Opportunity and You

Discusses criteria used in determining creditworthiness. Includes filmstrip, activity sheets, teacher's outline, and guide to deliver narrative. Federal Reserve Bank of New York, 1980. ($4.00 per set)

Getting Credit

Reviews the procedures for establishing credit. Contains filmstrip, narrative, learning assignments, class discussion, and vocabulary. Federal Reserve Bank of New York, 1981. ($4.00 per set)

Films

(Available from all 12 regional Federal Reserve Banks and Publication Services, Division of Administrative Services, Board of Governors of the Federal Reserve System, Washington, DC 20551.)

To Your Credit

Describes consumer credit regulations including the Equal Credit Opportunity Act, the Fair Credit Reporting Act, Truth in Lending, and the Fair Credit Billing Act. Explains the importance of creating a good credit record. Federal Reserve Bank of Philadelphia, 1978, 16mm color film, 15 minutes.

EFT: At Your Service

Introduces the concept of electronic fund transfer and explains the various EFT options available to consumers. Identifies consumer protection and responsibilities under the Electronic Fund Transfer Act. Includes a teacher's guide and activity masters. Federal Reserve Bank of Philadelphia, 1980, 16mm color film, 14 minutes.

Addresses of the Board and Federal Reserve Banks

Publications Services
Division of Administrative Services
Board of Governors of the Federal Reserve System
Washington, DC 20551

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Federal Reserve Bank of Boston
Boston, MA 02106

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Federal Reserve Bank of St. Louis
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Office of Public Information
Federal Reserve Bank of Minneapolis
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Minneapolis, MN 55480

Public Information Department
Federal Reserve Bank of Kansas City
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Kansas City, MO 64198

Department of Communications, Financial and Community Affairs
Federal Reserve Bank of Dallas
400 South Akard Street
Dallas, TX 75222

Public Information Department
Federal Reserve Bank of San Francisco
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San Francisco, CA 94120

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SECTION 1

An Overview of Consumer Credit

Introduction

Credit has become a very important part of modern-day life. Instead of waiting until they save cash, consumers may use credit to obtain desired goods and services now and pay later using future income. Section 1 will help students identify the benefits as well as the risks of using credit. Students will also learn how to use credit safely and recognize the signs of financial trouble. The overview will also provide students with a background for studying the consumer credit laws that protect consumers as they apply for and use credit.

Key Concepts

1. The availability of consumer credit allows individuals and families to buy needed or desired goods and services now using future income.
2. The granting of credit depends in part on a lender's confidence that a borrower will be able and willing to pay later for goods, services, or money received now.
3. Consumers should plan and control their purchases of goods and services using credit as carefully as their purchases using cash to avoid using more credit than they can repay.
4. Establishing and maintaining a record of using credit responsibly helps a consumer obtain both future credit and certain goods or services not available using cash, such as hotel accommodations and rental cars.
5. Comparing the costs and benefits of (1) using credit, (2) using available cash, or (3) saving until cash is available can help a consumer decide how and when to make a purchase.

Topic 1—What Is Consumer Credit?

Objective: Student can identify situations where consumers use credit. Student can define "credit" and give examples of public utility, incidental, closed-end, and open-end credit.

Materials Needed:
Reading 1—"What Is Consumer Credit?"
Credit Use Survey
Student Exercise 1

Directions:

1. Write the word "credit" on the chalkboard or poster paper. Ask students to write down a phrase of two or more words including the word "credit." Collect responses and tally the number of times each response is given. What do students associate most with the word "credit"? [Credit card, line of credit, good credit risk, open-end credit, credit rating, credit bureau, etc.]
2. Students will probably be familiar with credit cards, or open-end credit. They also may be aware of closed-end credit such as mortgage loans and automobile loans. Assign Reading 1, which defines four different types of consumer credit including the less formal incidental and public utility credit that most consumers use.
3. Assign Student Exercise 1 to test student understanding of the definitions of the four types of consumer credit. [See "Answer Key."]
4. Distribute the Credit Use Survey and go over the directions with students. You may want to assign the survey as homework so students can discuss credit use with their families. Tell students that Column IV is optional. Instead of recording actual monthly credit payments, students may leave Column IV blank or record typical or estimated monthly credit payments.

Topic 2—Why Do You Use Credit?

Objective: In a simulation, students will decide whether or not to use credit to make certain purchases. Student can identify situations when credit use is justified.

Materials Needed:
Simulation—"Would You Use Credit?"
Discussion Guide for "Would You Use Credit?"
Credit Use Survey (Topic 1)

Directions:

1. Divide class into small groups of four to six students each. Give each group the simulation and ask students to read the simulation directions. Because people's attitudes about using credit and how people use credit vary, there are no right or wrong answers. Students in each group should read situations 1-10 and discuss reasons to use credit and reasons not to use credit. The group then must decide what to do in each situation and select a spokesperson to explain the group's decisions to the class.

2. Call on group spokespersons to explain their decisions. Using the Discussion Guide, discuss the advantages or disadvantages of credit use in each situation. Emphasize to students that often there is a trade-off between the benefits of using/not using credit and the costs of using/not using credit.

3. Ask students to refer to their Credit Use Surveys (Topic 1) and give specific reasons why credit was obtained from each of the credit sources they have listed (convenience, shortage of cash, a means of purchasing very expensive items, a means of obtaining needed items, etc.). Individually, students may want to ask themselves whether credit use is justified in each instance.

Topic 3—How Much Credit Is Safe to Use?

Objective: Student can define and identify signs of overextension—using too much credit. Student can use guidelines recommended by lenders to determine how much credit is safe to use at different income and spending levels.

Materials Needed:
Student Exercise 2
Transparency 1—"Are You Using Too Much Credit?"
Reading 2—"Credit Guidelines"

Directions:

1. Ask students to identify the risks of using credit. [Consumers who use credit to make purchases risk using too much credit. A consumer who underestimates monthly expenses or incurs unexpected expenses may not have enough money to repay credit or make payments as agreed. This is called being "overextended." A consumer may also experience a reduction or loss of income. In either case, the consumer would have to reduce spending in order to make debt payments or he/she would not be able to repay as agreed.]

2. Assign Student Exercise 2. When students have completed the exercise, ask individual students to identify and explain why they underlined certain statements. [See "Answer Key."] Show students Transparency 1 and discuss the signs of overextension exhibited by Grabby Gerty and High-Living Hank.

Vocabulary

Closed-end Credit	One-time credit for a specific amount, usually for a large purchase and repaid in installments.
Consumer Credit	Credit used by individuals and families for personal, family, or household purposes.
Convenience Credit	Credit which is repaid by the consumer within 30 days or another specified period of time and on which there is no finance charge.
Credit	The promise to pay in the future in order to buy or borrow in the present.
Creditor	A person or business that regularly extends credit on which a charge may be imposed.
Credit Record	A history of credit use; also called a "credit history."
Discretionary Income	The portion of income that is left after a consumer has paid for essential items.
Finance Charge	The total of all charges imposed by a creditor for the use of credit.
Incidental Credit	An informal arrangement in which businesses and professionals provide credit for which there is no charge and no specific repayment plan.
Inflation	A general rise in the prices of goods and services.
Interest	A standard periodic charge for the use of credit which is one component of the finance charge.
Open-end Credit	A line of credit that may be used repeatedly up to a certain dollar amount and on which a charge may be imposed.
Overextension	Using more credit than is safe, given a consumer's income, expenses, and current debts.
Public Utility Credit	An informal credit arrangement with utility companies in which customers pay for services received in the past and involving no credit charges.
Purchasing Power	The amount of goods and services that can be purchased with a specified amount of money.

3. As a class, read Reading 2. Review with students the examples showing how consumers can estimate how much to spend on credit payments. Students may want to estimate how much they can safely spend on monthly credit payments based on their own incomes and expenses. Or have students practice using the lenders' guidelines to estimate how much is safe to spend on credit payments at higher and lower discretionary incomes.

Topic 4—Why Is Credit Important?

Objective: Student will identify the time during a person's life when spending needs generally exceed income. Student will know how to establish credit and some possible outcomes of not having a credit record.

Materials Needed:

Transparency 2—"Life-Cycle Spending and Earnings Patterns"
Case Study 1
Transparency 3—"How to Establish a Credit Record . . ."

Directions:

1. Show students Transparency 2 and discuss the Life-Cycle Spending and Earnings Pattern graph using the following questions:
   a. According to the Life-Cycle Spending and Earnings Pattern graph, what age group usually has spending needs which exceed income? [Spending needs generally exceed income until about age 35.]
   b. What are some of the potential spending needs for which people between the ages of 18 and 35 might use credit? [Automobiles, college tuition, houses, furniture, appliances, vacations, medical expenses.]
   c. Do people whose incomes are higher than their spending needs use credit? [As mentioned previously in this section, credit can be used for reasons other than a shortage of cash. The activities of Topic 5 describe why a consumer without a spending-earnings gap may use credit instead of cash.]
2. Compare spending needs as a percentage of income for specific age groups using the "empirical evidence"* for the Life-Cycle Spending and Earnings Pattern graph:

	Age of Household Head (in Years)					
	Under 25	25-34	35-44	45-54	55-64	65 and Older
Average after-tax income	$5,773	$9,969	$12,114	$13,069	$10,277	$5,764
Spending needs	$6,442	$9,550	$11,614	$11,789	$ 9,094	$5,399
Spending needs as percent of income	112%	96%	96%	90%	88%	94%

(Note: These data represent the most recent aggregate spending information available. Although actual spending and income levels have risen over time, the general relationship between spending and earnings during the life cycle is still valid.)

3. Emphasize to students that consumers eventually must repay credit used for spending needs listed in question b above. In the long run, spending cannot exceed income—consumers ultimately must pay for all of their purchases.

* U.S. Department of Labor, *Bureau of Labor Statistics Report* 455-4, Consumer Expenditure Survey Series: Interview Survey, 1972-73, Table 5, pp. 64-70.

4. Assign Case Study 1. Discuss students' responses to the questions following each case describing a consumer who is denied access to goods or services because of no prior credit use. [See "Answer Key."]
5. Use Transparency 3 to discuss ways young consumers or consumers who have not established credit in their own names can improve their chances of obtaining credit.

Topic 5—The Economics of Credit

Objective: Student will identify three major uses of income and three ways to pay for purchases. Student will know what to consider when deciding to postpone a purchase or make an immediate purchase using cash or credit.

Materials Needed:

Transparency 4—"Consumer Decides . . ."
Case Study 2
Reading 3—"The Credit Decision"

Directions:

1. Show students Transparency 4, which illustrates how a consumer uses income and how a consumer pays for purchases. Discuss the transparency with the following questions:
   a. After you purchase items on credit, can you "decide" how much of your income you will use to repay debt each month? [No, not always. On closed-end credit accounts, monthly payment amounts generally are predetermined. On open-end credit accounts, however, you may pay an amount ranging from the "minimum payment" to the full amount due.]
   b. How else can you use current income after you have paid for essential purchases—food, housing, transportation, etc.? [Current income can be (1) used to repay debt, (2) saved or invested , or (3) used to make additional purchases.)
2. Assign Case Study 2. Discuss how the consumer's decision to use credit depends on many elements—the item itself, its cost, the consumer's attitude about using credit or savings, interest rates, current debts, upcoming purchases, and changes in income, price levels, or the inflation rate. In each case, the consumer must decide whether it's worth incurring a debt to have the immediate use of goods or services purchased on credit. [See "Answer Key."]
3. Transparency 4 identified the three sources of funds available to consumers for spending: current income, savings, and credit. Assign Reading 3, which describes what a consumer may consider when deciding how and when to make a purchase. Discuss students' answers to questions about Joan Richards' purchase of a freezer. [See "Answer Key."]

   (Note: You may wish to discuss the effect of taxes on a purchase using cash or credit. Under our current tax laws, Joan must pay taxes on interest earned on her savings; interest paid on a loan is tax-deductible. Therefore, taxes may reduce the value of her savings and reduce the costs of using credit. In this case, tax considerations would increase the attractiveness of buying now [with credit or savings] rather than waiting and may alter the trade-off between using credit or savings.)

Answer Key

Pretest

1. *False*. To be granted credit, consumers must provide evidence that they are able and willing to repay credit.
2. *True*. Because the electricity is used before the consumer pays for it, credit has been granted. This is an example of public utility credit.
3. *False*. Although some credit arrangements do require a formal application, public utility credit and credit granted by professionals and small businesses (incidental credit) usually do not.
4. *False*. Even a consumer who can pay cash may not want to disturb savings, or the cash may not be readily available. In addition, using and repaying credit as agreed may help a consumer obtain credit in the future.
5. *False*. Incidental and public utility credit do not involve a cost. "Convenience credit" allows a consumer to repay in 30 days, for example, without incurring additional finance charges.
6. *True*. Without credit, many consumers would be unable to purchase cars, appliances, furniture, etc., which are considered necessities today. If credit were not available, few people could ever afford to buy a home. In addition, many services such as hotel accommodations and rental cars may only be obtained by using a credit card.
7. *True*. A consumer who is "overextended" cannot repay credit as agreed. Higher finance charges, a poor credit record, and legal action may result.
8. *True*. Earnings from overtime work and bonuses are not reliable. A consumer who relies on them to pay credit bills risks not being able to pay.
9. *False*. At middle and higher incomes, 20% of one's net (takehome) income may not be too much to spend on credit bills. However, at lower incomes a higher percentage of a consumer's income is used to buy "essentials," and 20% of income may be too much to spend to repay credit.
10. *True*. When prices are rising due to inflation, a consumer may "save" money by using credit to take advantage of a lower purchase price.

Topic 1, Student Exercise 1

1. Open-end
2. Public utility
3. Incidental
4. Closed-end
5. Closed-end
6. Incidental
7. Open-end
8. Open-end
9. Closed-end
10. Open-end

Topic 3, Student Exercise 2

Credit Profile 1

Grabby Gerty loves having a Bargains Galore credit card! She can go shopping whenever she wants and buy whatever she wants even if she's short of cash. Bargains Galore has terrific sales, and Grabby Gerty's monthly credit bill is always high. She usually pays only the "minimum payment" required. Lately, Grabby Gerty has had little money left after paying all her credit bills. She even "charges" groceries at Bargains Galore. When her monthly credit bill arrives from Bargains Galore, she sees she will have to skip making payments to her doctor and the bank to make even the minimum payment.

Credit Profile 2

High-Living Hank is proud of all his plastic money—credit cards. He can charge just about anything he wants. Every month, though, Hank has a pile of bills and the job of figuring out how he will pay them. Usually, Hank works enough overtime to make ends meet. He also has a savings account that he dips into if he's a little short of cash. He and his wife are saving toward a down payment on a vacation home. It's been five years now, but they still have not saved enough money. Hank has been thinking about getting a debt consolidation loan to pay off all his bills. It would be a lot easier to pay just one bill.

Topic 4, Case Study 1

Case 1: Although the Smiths are financially responsible, they have no history of credit use that demonstrates their responsibility. Lenders generally want to know how you've handled financial obligations in the past—especially if you apply for a major loan. The Smiths could have established a credit record by using one or more open-end credit accounts responsibly. They also could have obtained a loan to make a major purchase, such as their new car.

Case 2: If a consumer does not have a record of credit use, a lender might require a larger down payment or a cosigner. Or, the lender might even refuse to make the loan. Firms that rent or lease goods (i.e., car rental agencies, hotels, etc.) often want evidence that a customer is responsible and trustworthy to minimize chances of theft, damage, or nonpayment. Being approved for a national bank credit card (VISA, MasterCard) is often considered as evidence that a person is financially responsible.

Topic 5, Case Study 2

Case 1: No, Mrs. Johnson did not save money by postponing her purchase. By waiting she had to pay more to buy the television than if she had used credit and paid finance charges. However, by saving one additional month she would have the $330 in cash. It is possible that not incurring a debt and not being responsible for a monthly payment are more important to Mrs. Johnson than the money she would save using credit.

Case 2: Mr. Gray will eventually pay $323 for the golf clubs, including interest on his loan. If he waited a year with inflation at 10%, he would probably have to pay $330—so he might figure that he saved $7 by borrowing. If he put $26.94 per month into a savings account at 6% interest (compounded monthly), however, he would have $334 in a year. He could then buy the clubs for $330 and still have $4! In this case, the purchase decision depends on how Mr. Gray feels about using credit (and having a monthly payment) and how much he wants to have the use of the clubs as he pays for them.

Topic 5, Reading 3

1. If Joan waits a year or so to save enough money to buy the freezer, its purchase price may change. If she expects the price to go up, she should consider this extra cost. If she postpones the purchase, she will also forgo a potential savings of $100 in food costs for the year. On the other hand, if she waits until she has the additional savings, she will avoid committing herself to a monthly payment. Her savings will also remain intact.
2. If Joan uses accumulated savings, she will avoid committing herself to a fixed monthly payment. She will forgo earning interest on her savings at a rate of 6% per year, whereas the loan would cost 10% per year. If Joan promised to "pay herself" the $26.25 each month, she will repay the "borrowed" savings within a year. From a financial standpoint, she is better off using her savings. On the other hand, Joan may prefer the discipline provided by having to make loan payments instead of saving the same amount of money each month. In addition, by using credit she will establish a credit history. On this basis, it may be worthwhile for her to use credit.

Pretest

Directions: Circle "T" if the statement is true; circle "F" if the statement is false.

T F 1. Anyone who wants credit and is of legal age may obtain credit.

T F 2. By billing consumers this month for electricity used last month, power companies grant credit to consumers.

T F 3. All creditors require a consumer to complete an application form before granting credit.

T F 4. A consumer should always avoid buying now using credit if he/she can pay cash.

T F 5. A consumer pays more to obtain goods or services whenever credit is used.

T F 6. For the average consumer today, access to credit is a necessity.

T F 7. Using too much credit is one of the greatest risks of using credit.

T F 8. A consumer who relies on "overtime" pay and bonuses to pay credit bills may be in financial danger.

T F 9. If a consumer spends 20% or less of net monthly income to pay credit bills (not including mortgage payments), he/she is not using too much credit.

T F 10. It may cost less to make a purchase now using credit than to postpone a purchase and pay cash.

What Is Consumer Credit?

You pay a bill in January for electricity you used in December. A statement arrives in the mail for medical services you obtained last month. You write a check for $20.00 as a "minimum payment" on a $150.00 department store bill. With a bank loan you purchase a new car.

All of these are examples of using credit—paying later for goods or services obtained now. "Consumer credit" is credit used only for personal, family, or household purchases. Credit arrangements can be formal or informal. A specified amount of credit may be granted or credit may be "open-ended." A consumer can obtain credit only when a creditor has confidence that he/she is both able and willing to pay later for goods or services received now. You may pay for the privilege of using credit, or credit may be free. The four common types of credit used by consumers are described below.

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1. Public utilities credit

Power, water, gas, and telephone companies generally charge customers for their services after they have been used. How much you pay for electricity, for example, depends on how much you use. By allowing customers to pay later, utility companies are granting credit even if there are no formal credit agreements or credit charges. Consumers, however, may be required to pay a deposit before obtaining services initially from a utility company. In addition, a "penalty" charge may be added if a bill is not paid promptly.

2. Incidental credit

All of us have probably had a doctor or dentist appointment we did not pay for until later. Professionals and small businesses often do not demand immediate payment. If a credit arrangement involves no extra costs and there is no specific repayment plan, it is called "incidental credit."

3. Closed-end credit

Mortgage loans, automobile loans, home improvement loans, and installment loans for purchasing furniture or appliances are examples of "closed-end" credit. Closed-end credit is used for a specific purpose and is for a specified amount. An agreement, or contract, lists repayment terms—the number of payments, payment amount, and how much the credit will cost. The cost of credit may vary depending on state and local laws, general interest rates, price levels, the availability of credit, the demand for credit, and the creditor's assessment of the borrower's creditworthiness.

4. Open-end credit

Using a credit card issued by a department store, using a bank credit card (VISA, MasterCard) to make purchases at different stores, "charging" a meal at a restaurant, or using "overdraft" protection are all examples of "open-end" credit. Unlike closed-end credit, you do not apply for open-end credit for a single purchase. Rather you can use it to make whatever purchases you wish if you do not exceed your "line of credit"—the maximum amount of credit you can use. You may have to pay interest—a periodic charge for the use of credit—or other finance charges. Some creditors allow you 30 days to pay the bill in full and not incur any interest charges. This type of credit is called "convenience credit."

Credit Use Survey

Directions: List examples of the four types of credit you or your family use (Column 1). Under Columns II, III, and IV (optional), describe how you use and repay credit.

I **Credit Sources**	II **How often is credit used?**	III **How is credit repaid?**	IV **How much is spent on monthly credit payments?**
PUBLIC UTILITY Ex. City water 1. 2.	Every day	Paid quarterly	Approximately $30.00
INCIDENTAL 1. 2.			
OPEN-END 1. 2.			
CLOSED-END 1. 2.			

Student Exercise 1

Directions: Identify the type of credit described in each of the following examples and circle your answer.

1. A consumer makes purchases at All Goods Department Store using an All Goods credit card.

   public utility incidental closed-end open-end

2. A consumer pays a bill for long-distance telephone calls made last month.

   public utility incidental closed-end open-end

3. A doctors' office allows patients to pay their bills in installments but does not charge interest on the unpaid balance.

   public utility incidental closed-end open-end

4. A loan from a credit union is paid back in 24 bimonthly payments.

   public utility incidental closed-end open-end

5. A contract is signed that states the terms and conditions of paying an orthodontist's fee.

   public utility incidental closed-end open-end

6. A local hospital sends a patient a bill for $50 for emergency room treatment.

   public utility incidental closed-end open-end

7. A consumer pays for a dinner using a credit card issued by the restaurant.

   public utility incidental closed-end open-end

8. A bank credit card is used to make purchases at several retail stores.

   public utility incidental closed-end open-end

9. Furniture, Inc., requires customers to sign a contract each time they purchase a new item.

   public utility incidental closed-end open-end

10. An "overdraft protection" agreement allows a consumer to write a $150 check when his account balance is only $100.

    public utility incidental closed-end open-end

Would You Use Credit?

Directions: Decide if you would use credit to make the following purchases. In the appropriate box, give the reasons for your decision.

1. *Would you use credit* to buy a home or pay for a college education?
2. *Would you use credit* to purchase appliances, furniture, etc., for a home?
3. *Would you use credit* to pay overdue bills?
4. *Would you use credit* to purchase gasoline or food?
5. *Would you use credit* instead of cash or checks to make several purchases in one store?
6. *Would you use credit* to purchase an item which costs $8.50?
7. *Would you use credit* to purchase an item on sale?
8. *Would you use credit* to pay for a vacation?
9. *Would you use credit* if you couldn't save enough money to buy something you wanted?
10. *Would you use credit* to make a purchase even if you could pay cash?

Yes	No	Maybe

Discussion Guide for "Would You Use Credit?"

1. Most people could never buy a home unless they used credit. Similarly, many people could never attend college if they couldn't obtain loans to be repaid later using future earnings.
2. If you can make the payments, using credit will allow you to have the use of the furniture or appliances as you pay for them. You may even save money by buying now on credit, depending on the interest rate charged and the expected change in the price of the item.
3. It is generally not a good idea to use credit to pay overdue bills. Bill-paying problems usually can be solved by reducing spending, increasing income, or negotiating with creditors for smaller but regular payments.
4. Most consumer credit counseling services recommend not using credit to buy perishable items. Not only is it difficult to keep track of what you have spent, but it's difficult psychologically to pay for something after you have used it. You may want to use "convenience credit" to purchase gasoline or food and then pay for those items in full on a monthly basis.
5. It may be more convenient to use credit than to write several checks, and it is safer than carrying large amounts of cash. You may not make purchases as carefully, however.
6. Consumer credit counselors recommend not using credit to purchase items costing less than $25. It may be difficult for you to keep track of small credit purchases. Some consumers are not as careful in making their purchase decisions if they use credit to buy lower-priced items. Using credit instead of cash, however, may be more convenient, safer, and in some cases less expensive (taking advantage of a reduced price, eliminating a second shopping trip, etc.).
7. If you plan to purchase the item sometime, you may save money using credit to buy it now rather than waiting to pay cash. Whether or not you would save money depends on how much the credit costs and how you will repay it.
8. If you use credit to pay for a vacation, you'll need to have money available to pay future credit payments. If the monthly credit payments will fit into your budget, taking a vacation now (when you want to) and paying later may be justified.
9. If you cannot afford to save (not spend) a certain amount of money each month toward a purchase, you probably can't afford to buy it on credit. Many people, however, find it easier to make payments each month (forced savings) than to save the same amount of money each month.
10. Credit can be used for many reasons besides a shortage of cash. You may use credit to establish a record of responsible credit use or for the convenience and safety it offers. Also, by making a purchase now using credit, you might pay less money for an item than if you had waited to pay cash.

Student Exercise 2

Directions: Read the "credit profiles" below. Underline any statement that may indicate the consumer is using more credit than he or she can use safely.

Credit Profile 1

Grabby Gerty loves having a Bargains Galore credit card! She can go shopping whenever she wants and buy whatever she wants even if she's short of cash. Bargains Galore has terrific sales, and Grabby Gerty's monthly credit bill is always high. She usually pays only the "minimum payment" required. Lately, Grabby Gerty has had little money left after paying all her credit bills. She even "charges" groceries at Bargains Galore. When her monthly credit bill arrives from Bargains Galore, she sees she will have to skip making payments to her doctor and the bank to make even the minimum payment.

Credit Profile 2

High-Living Hank is proud of all his plastic money—credit cards. He can charge just about anything he wants. Every month, though, Hank has a pile of bills and the job of figuring out how he will pay them. Usually, Hank works enough overtime to make ends meet. He also has a savings account that he dips into if he's a little short of cash. He and his wife are saving toward a down payment on a vacation home. It's been five years now, but they still have not saved enough money. Hank has been thinking about getting a debt consolidation loan to pay off all his bills. It would be a lot easier to pay just one bill.

Are You Using Too Much Credit?

I'll pay next month . . .

All I have to pay is the "minimum amount" . . .

I'll have to dip into savings to pay bills just this month . . .

I can count on my "overtime" to pay the bills . . .

I can always charge my groceries and gasoline if I'm short of cash . . .

Why can't I save any money?

I don't even know how much I owe anymore . . .

Credit Guidelines

Whether a consumer is considering using credit for the first time or is experiencing symptoms of credit overuse, it is important to know how much credit is safe to use.* One credit guideline used by lenders is based on a consumer's disposable, or net monthly income (take-home pay after taxes and other deductions). The rule would be for a consumer to spend no more than 20% of net monthly income on debt payments or credit bills (not including housing payments). An example follows of how this guideline may be used to determine a safe amount of money to spend on credit:

Example 1
Joe's net monthly income is $2,000. How much can he safely spend on monthly credit payments, not including his mortgage payment?

20% of net monthly income =
.20 x $2,000 = $400

In some circumstances, lenders would recommend that a consumer spend less than 20% of net monthly income on credit payments. At middle and lower incomes, a greater percentage of income is used to pay for "essentials" such as housing, food, clothing, transportation, and medical expenses. Another credit guideline lenders use is based on a consumer's "discretionary" income—that portion of income not needed for essentials. Using this guideline, they recommend that consumers spend no more than one-third of their monthly discretionary income on credit payments. Example 2 illustrates how a consumer may use this guideline to determine how much money to spend on monthly credit payments.

* These guidelines are based on actual guidelines that lenders use to decide if applicants will be granted or denied credit.

Example 2
Jim's net monthly income is $1,500. He spends the following amounts each month for essential items:

Mortgage loan	$450
Utilities	100
Food	200
Transportation	100
Clothing	25
Medical expenses	25
TOTAL	$900

What is Jim's monthly discretionary income?

Discretionary income = Net Income — Spending on essentials
Discretionary income = $1,500 — $900
= $600 per month

How much can Jim safely spend on other credit payments each month?

1/3 of discretionary income =
1/3 of $600 = $200

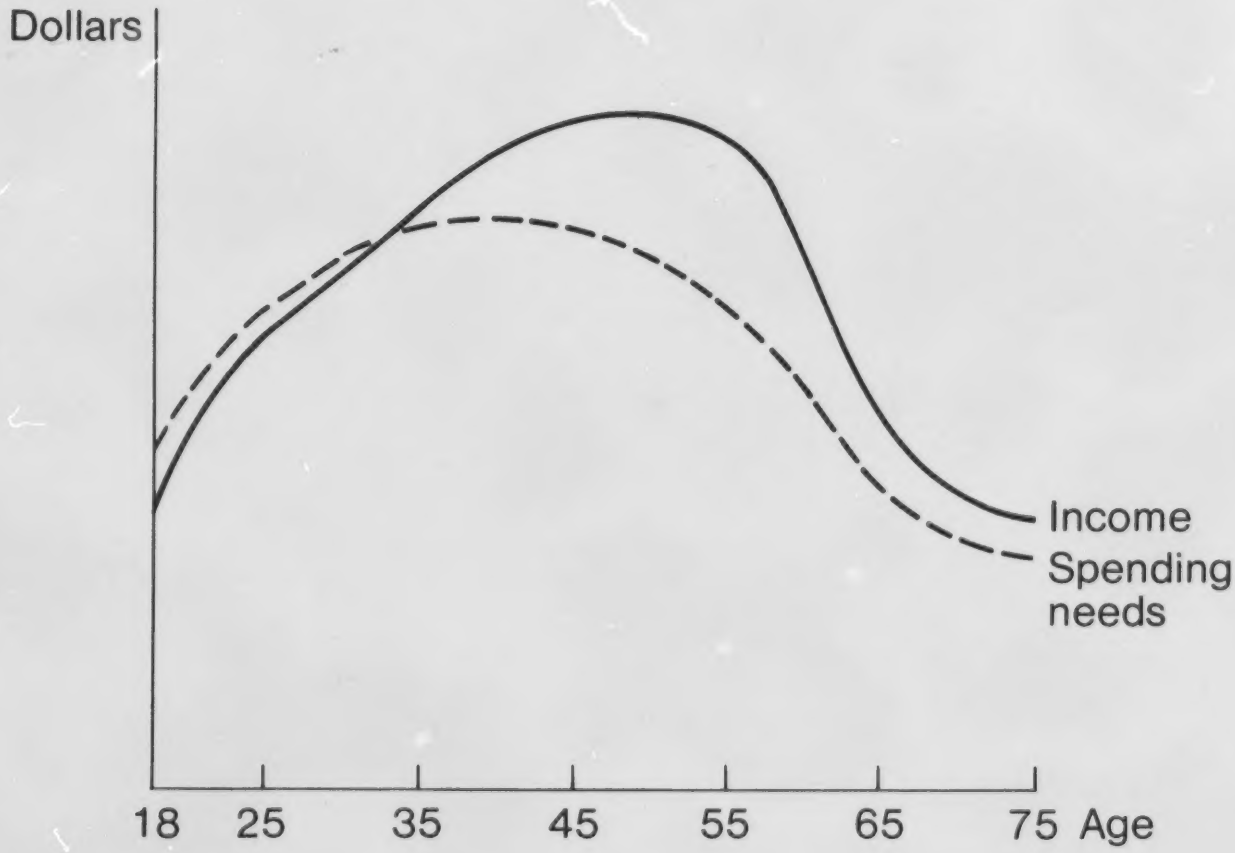
What percentage of his net monthly income can Jim spend safely on credit (not including housing) payments?

$200 ÷ $1,500 = .133
= 13%

In Jim's case, 20% of net monthly income, or $300, is too much to spend on credit payments because of his essential spending needs.

As these examples show, people have different financial situations. What is a safe amount of money to spend on credit for one person may be too much for another person to spend. People's attitudes about using credit and being in debt also vary and may influence how much credit they use.

Life-Cycle Spending and Earnings Patterns



Case Study 1

Case 1:
John and Jane Smith have been house-hunting for several months. They finally decide on a three-bedroom rambler and apply at a savings and loan association for a mortgage loan to purchase it.

Both John and Jane have jobs, and their combined income is sufficient for them to make the required monthly payment. The Smiths have no outstanding debts because they always pay cash. They even paid cash to buy their new car. Over the last few years they have saved a substantial down payment.

A week later the Smiths are notified by the savings and loan association that in order to be approved for the mortgage loan, they will need a cosigner.

Why do you think the Smiths are required to have a cosigner?

Case 2:
Alfred Jones flew to New Orleans to attend his brother's wedding. Knowing his family would be very busy, he did not ask anyone to meet him at the airport. Instead, he planned to rent a car to use while in New Orleans. He has no nationally recognized credit card but is prepared to pay cash for the rental car.

The car rental agency refuses to rent him a car, even though they have several cars available.

Why do you think Alfred is unable to rent a car?

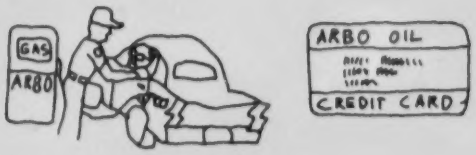
How to Establish a Credit Record . . .

1. **Pay bills on time** for goods and services already used such as electricity, telephone, doctors, and dentists.

2. **Pay monthly rent payments on time.**

3. **Use lay-away plans or 90-day interest-free plans** available at local retail establishments.

4. **Obtain** (if you have a steady income) **a limited-use credit card** or one with a credit maximum. Pay bills promptly.

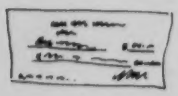


5. **Establish and use a transaction account** as evidence you can handle your money responsibly.

Consumer Decides . . .

How to Use Household Income

Pay Debts
(Past Spending)



Make New Purchases
(Current Spending)

Save, Invest
(Future Spending)

and . . .

How to Pay for New Purchases

Credit
(Future Income)

Cash
(Current Income)

Savings
(Past Income)

Case Study 2

Case 1
Mrs. Johnson doesn't have enough cash to pay for a $300 television set. She could buy it on credit by agreeing to make 12 monthly payments of $26.37 each. The total cost then would be $316.44. Instead she decides to put $25 a month in the bank until she has saved enough money to make the purchase. One year later Mrs. Johnson has saved $306.82, which includes the $300 plus interest paid at a rate of 6% per year. When she goes back to the store, she finds that the same television set now costs $330. Its price has gone up 10%—the current rate of inflation.

Did it "pay" for Mrs. Johnson to postpone her purchase?

Case 2
Mr. Gray began playing golf recently. Now he wants to buy his own golf clubs. He finds some clubs he likes at Ace's Sporting Goods which cost $300. He doesn't have $300 in cash, and he figures it would take him approximately one year to save that amount. With an inflation rate of 10%, he estimates that the clubs will cost 10% more a year later, or $330. Mr. Gray applies for and is granted a loan for $300 at an interest rate of 14% per year. He agrees to repay the loan in 12 monthly payments of $26.94 each.

Is it "rational" for Mr. Gray to use credit to buy his golf clubs now instead of waiting a year?

The Credit Decision

Using credit to purchase goods or services may allow consumers to be more efficient, more productive, or have more satisfying lives. Of course, credit must be repaid. Using credit increases the amount of money a consumer can spend to purchase goods and services now and decreases the amount available to spend in the future. Many people expect their incomes to increase and, therefore, expect to be able to make payments on past credit purchases and still make new purchases.

The decision to use credit or cash to make a purchase depends upon many elements—such as the price of the item, how soon the item is needed, the cost of using credit, and the cost of postponing a purchase. For example, if you need a car for transportation to and from work, you could either buy one now using savings or credit or postpone the purchase until you have saved the necessary amount in cash.

Some questions to ask before deciding how and when to buy a car include:

- Do I have the cash needed to make this purchase?
- Do I want to use my savings to make this purchase?
- Could I postpone the purchase? What are the costs of postponing the purchase? (Alternative transportation costs; a possible increase in the price of the car.)
- What are the dollar costs of using credit? Psychological costs? (Interest; other finance charges; being in debt and responsible for a monthly payment.)

If you decide to use credit, the benefits of making the purchase now (increased efficency or productivity, a more satisying life, etc.) should outweigh the costs (financial and psychological) of using credit. In the situation described below, consider the advantages and disadvantages of (1) buying now with cash, (2) buying now using credit, or (3) postponing the purchase. Then answer the questions that follow.

Joan Richards wishes to buy a freezer which today costs $300. She estimates that having a freezer by summer will save her $100 in food costs this year. She can purchase food on sale and in larger quantities, and she can preserve vegetables from her garden. Operating a freezer will, however, increase her electricity bill. She may purchase the freezer using one of the following options:

Option A Buy the freezer now using $300 she currently has in a savings account earning interest at the rate of 6% per year.

Option B Buy the freezer now using credit and paying the creditor interest at the rate of 10% per year. She would pay for the freezer in 12 monthly payments of $26.25 each.

Option C Postpone the purchase until she saves an additional $300. Her savings earn interest at the rate of 6% per year.

Questions

1. What things should Joan consider in deciding whether to buy the freezer now or later?
2. If Joan wants to buy the freezer now, what things should she consider in deciding whether to use credit or pay cash?

YOUR CREDIT RIGHTS

SECTION 2

The Equal Credit Opportunity Act

Introduction

The Equal Credit Opportunity Act, passed in 1974 and amended in 1976, prohibits creditors from treating one credit applicant less favorably than another because of the applicant's age, sex or marital status, race, color, religion, national origin, source of income, or the exercise of rights under the federal consumer credit protection laws. Through a simulation, students learn what types of information creditors use to determine whether an applicant is able and willing to repay. Students will also learn what restrictions the law places on information that creditors may obtain and use to evaluate applicants. Other discussion topics are the special credit problems of women, divorced persons, and the elderly, and how the Equal Credit Opportunity Act helps them to establish credit. Using case studies and flow charts, students learn what a consumer can do if he or she believes credit has been denied on the basis of "prohibited factors."

Key Concepts

1. A creditor considers a consumer a "good credit risk" if the information obtained from the credit application, credit report, or interview indicates he/she is willing and able to repay.
2. Creditors use the "three Cs of credit"—capacity to pay, character, and collateral—to evaluate an applicant's ability and willingness to repay credit.
3. A creditor cannot deny credit on the basis of an applicant's age, sex or marital status, race, color, religion, national origin, receipt of public assistance, or a "good faith" exercise of rights under the federal consumer credit laws.
4. Credit cannot be denied because an applicant's income is derived from part-time employment, alimony, child support payments, or public assistance if that income is reliable. Credit can be denied if income—from whatever source—is insufficient.
5. A creditor must disclose the reason(s) why a consumer is denied credit. This gives the consumer an opportunity to dispute a creditor's reason for denying credit. There often are steps a consumer can take to improve his/her chances of obtaining credit in the future.

Topic 1—Who's a Good Credit Risk?

Objective: Student will learn what characteristics indicate or affect a credit applicant's ability or willingness to repay. In a simulation, students make decisions to grant or deny applicants credit and identify information that indicates creditworthiness.

Materials Needed:
Transparency 1—"The 3 Cs of Credit"
Simulation—"Who's a Good Credit Risk?"

Directions:

1. Every credit account opened or loan granted represents a potential loss for the credit grantor. Creditors cannot predict all losses. For example, credit payments that may have fit easily into a consumer's budget may be missed if that consumer loses a job or incurs unexpected expenses. Explain to students how creditors deny credit to applicants who appear unable to repay and how they grant credit to those who are "good credit risks." Show Transparency 1, which defines the "three Cs of credit" that many creditors use to determine whether an applicant is a good credit risk. Use the questions listed on the transparency to illustrate how a creditor uses certain information to assess an applicant's "capacity to pay," "character," and "collateral."
2. Divide the class into four groups and distribute the simulation. Ask students to read the simulation directions carefully and then to go ahead and make their credit decisions.
3. After each group has made its loan decisions, have one student from each group record those decisions on the chalkboard. Use a chart similar to the one below:

	Group 1	Group 2	Group 3	Group 4
Applicant 1	*Approved*	*Denied*	*Approved*	*Approved*
Applicant 2				
Applicant 3				
Applicant 4				

(Note: Students' decisions will not necessarily be right or wrong. Students have not been given complete information about each applicant, and their decisions will also reflect their past experiences, attitudes, values, etc. Similarly, individual creditors who have had different experiences with borrowers will make different decisions. Also, each creditor sets somewhat different standards for granting credit. A credit applicant who is denied credit by one creditor may obtain credit from another.)

4. Show Transparency 1 again. Ask students to decide whether information given for applicants 1-4 in the simulation indicates or affects the applicant's capacity to pay, character, or collateral. For example, "has ten charge accounts" is information given about Applicant 1. Having ten charge accounts indicates he/she has used credit in the past (character); however, current credit bills may be too high to justify additional credit use (capacity to pay). Explain to students that some of the information provided for applicants 1-4 may *not* indicate or affect the ability or willingness to repay. [See "Answer Key."]
5. Discuss student responses in the activity above using the following questions:
   a. Which pieces of information provided for applicants 1-4 refer to characteristics which never change or cannot be changed easily? [62 years old, white, divorced, female, 21 years old, Mexican-American.]
   b. Does working part-time or receiving public assistance necessarily mean an applicant does not have sufficient

Vocabulary

Adverse Action — Any action taken by a creditor denying a consumer credit in the future, including rejecting an application or closing or changing the terms of an existing account.

Class-action Suit — A lawsuit brought on behalf of many people, all of whom suffered the same wrong.

Collateral — Property or other valuables pledged by a consumer as security for a loan.

Cosigner — Another person who signs a loan and is liable for repayment if the borrower defaults.

Credit Discrimination — A creditor who denies credit or treats a consumer less favorably because of his/her race, sex, religion, marital status, etc.

Credit Life and Health Insurance — Insurance purchased by a consumer which repays credit in the event of his/her death or disability.

Credit-scoring System — A statistical method used by large creditors to rate credit applicants in which "points" are assigned to various factors related to creditworthiness.

Creditworthiness — A consumer's past and future ability and willingness to repay credit as determined by a creditor.

Down Payment — An amount of money which a consumer pays toward the purchase of goods; the remaining purchase price is then loaned to the consumer.

Elderly Applicant — A credit applicant who is 62 years or older.

Joint Account — An open-end credit account which may be used by more than one person and for which all potential users are liable for repayment.

Judgment — A court decision that someone is entitled to payment in a fixed amount from another person.

Judgmental System — A nonstatistical method of evaluating creditworthiness involving a creditor's judgment of an applicant's ability and willingness to repay.

Prohibited Factors — Factors or characteristics about a person which cannot be used by a creditor as a basis for denying credit (age, sex, marital status, race, religion, color, national origin, receipt of public assistance, or exercise of rights under federal consumer credit protection laws).

Punitive Damages — Damages which the court may award which are over and above the amount that would compensate the consumer.

Secured Credit — A credit arrangement in which a consumer pledges goods or property as collateral which may be seized by the creditor in case of default.

Unsecured Credit — A credit arrangement in which no collateral is pledged. In case of default, the creditor must sue for repayment, but has no special rights to specific goods or property.

income to qualify for credit? [No, such information indicates only the *source* of income not the amount of income.]

c. Does being divorced necessarily mean a person is not creditworthy? [No. Statistics show that divorced persons may default more often than married persons. However, the fact that a consumer is divorced does not indicate anything about that particular consumer's ability and willingness to repay credit.]

6. Write the word "judgmental" on the chalkboard. Indicate to students that they used a judgmental system in the simulation to determine creditworthiness. Ask students to try to explain what is meant by a judgmental system based on their experiences in making credit decisions in the simulation. [A creditor or loan officer makes an independent and personal decision about an applicant's ability and willingness to repay credit. There may be some "fixed" requirements, such as a minimum income needed to quality for a loan; however, the decision to grant or deny credit is based on the creditor's or loan officer's judgment regarding the applicant's ability and willingness to repay. In making this judgment, the creditor or loan officer will be influenced by his/her experiences with other borrowers and by the type and amount of credit being requested.]

   Write the word "empirical" on the chalkboard. Explain to students that when many different people make the credit decisions for one creditor, generally another system is used to evaluate applicants. This is an "empirical" system, also called "credit-scoring." In a credit-scoring system, a certain value or a certain number of "points" is assigned to various factors that have proven to be reliable predictors of repayment. Credit is granted if an applicant receives a required number of "points."

   (Note: Since passage of the Equal Credit Opportunity Act, credit-scoring systems must be statistically reliable and cannot discriminate against persons because of their race, color, religion, national origin, sex or marital status, or receipt of public assistance.)

Topic 2—The Equal Credit Opportunity Act

Objective: Student can identify nine factors, including age, sex, and marital status, that cannot be used as a basis for denying credit. By examining a sample credit application, student will know when a creditor may ask about an applicant's age, marital status, alimony or child support payments, or obtain information about a spouse or former spouse.

Materials Needed:
Reading 1—"Your Equal Credit Opportunity Rights"
Transparency 2—Credit Application

Directions:

1. In the simulation activity of Topic 1, students assumed the roles of creditors making credit decisions. Explain to students that until 1974, creditors were free to make credit decisions on any basis they wished (although federal laws applied to certain housing loans). With the passage of the Equal Credit Opportunity Act, creditors may still establish certain criteria for granting credit—such as a minimum income or length of time on a job. However, the standards they use must be applied uniformly to all applicants regardless of their race, color, religion, national origin, sex or marital status, age, source of income, or the exercise of rights under the federal consumer credit protection laws.
2. Ask students if consumers have the "right" to receive credit. [No, consumers only have the right to be judged on the same basis as other persons applying for credit. They may be denied credit for business reasons (insufficient income, poor credit history, etc.), but they cannot be denied credit because of their race, color, religion, national origin, etc.]
3. Distribute Reading 1, which summarizes the provisions of the Equal Credit Opportunity Act. As a class, read and discuss the list of rights and provide definitions and clarifications as needed. Point out to students the dual purposes of the Act: To prevent credit discrimination and to help qualified applicants obtain credit. Because the Act requires disclosure of the reason(s) for credit denial, a consumer can dispute credit denials and/or negotiate for new credit terms in order to obtain credit.
4. One source of information used by lenders to make credit decisions is the credit application. Show Transparency 2 and explain that it is an application form recommended for use by the Federal Reserve System. Discuss the credit application using the questions below:

   a. Is the following information requested: sex, race, religion, national origin? [No. Credit applicants cannot be asked to reveal such information (except for monitoring purposes in real estate credit).]

   b. Why does the application form include a space for the applicant's birthday if a creditor cannot use age as a basis for denying credit? [Creditors need to know an applicant's age in order to verify that he/she is old enough to enter into a legal contract.]

   c. Does disclosure of the number and ages of dependents allow creditors to guess an applicant's marital status? [Perhaps, but such information is important in judging whether an applicant's income is sufficient to repay credit.]

   d. When is a credit applicant required to reveal alimony, separate maintenance, or child support payments? [Payments made by a spouse or former spouse must be disclosed if an applicant will be relying on them to repay credit. In evaluating an applicant, a creditor may consider the reliability of such payments as well as the creditworthiness of the person making the payments.]

   e. What income could a credit applicant list under "other income?" [Pension or retirement income, aid for dependent children, social security payments, welfare payments, etc. A creditor must consider an applicant's other income—if it is reliable—regardless of the source. Again, a credit applicant need not list income that will not be relied on for repayment.]

   f. Why is an applicant for joint credit required to reveal his/her marital status and information about the joint applicant or user? [The creditor needs this information in order to record and report the account's payment history in both spouse's names.]

   g. On a secured loan, specific property may be repossessed by a lender if the borrower does not pay. Applicants for secured credit must always reveal their marital status. Why? [This information is needed because a spouse or a former spouse may have a legal interest in the property.]

Topic 3—Eighteen or Sixty-Two—What Are Your Credit Rights?

Objective: Student can distinguish between credit denied illegally on the basis of an applicant's age and credit denied because of insufficient income or lack of a good credit history. Student will know how creditors must rate an elderly person's age if they use a credit-scoring system.

Materials Needed:
Case Study 1
Transparency 3—"Credit and Age"
Transparency 4—"Scoring Age"

Directions:

1. Assign Case Study 1, which describes three instances of credit being denied to younger or older consumers. As a class, discuss student responses to the questions following each of the three cases. [See "Answer Key."] Be sure students understand the difference between denying credit because of a person's age and denying credit because of insufficient income or lack of a credit history.
2. Using Transparency 3, discuss "rules" that govern how creditors can and cannot use an applicant's age to deny credit or change credit terms. Students should be asked to identify the "rules" which apply to each case in Case Study 1. [Case 1: none; Case 2: rules 2, 3; Case 3: rules 1, 4.]
3. In the past, some creditors used age routinely to determine creditworthiness. They believed that applicants under 30 years of age were more likely to default than older applicants (those 30-50 years old). They also believed older persons (60-65 years old) were more likely to default than younger persons because of health reasons, retirement, etc. Show Transparency 4, which illustrates how age was "scored" in a hypothetical credit-scoring system before the Equal Credit Opportunity Act. In this example, persons over 59 years of age are given fewer points for their age than persons 30-59 years of age. Under the current law and regulations, creditors must assign at least as many points to an elderly person's age (62 and over) as they assign to the age of any person who is younger. Ask students what needs to be changed on Transparency 4 in order for the credit-scoring system to comply with the age provisions of the Equal Credit Opportunity Act. Use a grease pencil to make changes on the transparency. [See "Answer Key."]

Topic 4—The Credit Rights of Women

Objective: Student will be able to identify instances in which credit is denied because of an applicant's sex or marital status. Student will know how the Equal Credit Opportunity Act helps women establish and protect their credit histories.

Materials Needed:
Case Study 2
Transparency 5—"Credit Rights of Women"
Transparency 6—"Freedom of Choice"
Reading 2 (Optional)—"The Problem of the Disappearing Credit History"

35

Directions:

1. Divide the class into small groups and assign Case Study 2. Each group should read the three cases and answer the questions regarding whether credit has been denied on the basis of the applicant's sex or marital status. When students have completed their work, ask each group to tell the class how it answered the questions and to explain why. [See "Answer Key."]
2. Show Transparency 5, which lists ten "rules" pertaining specifically to the credit rights of women. Ask students to identify provisions which apply to the situations described in Case Study 2. [Case 1: rules 1, 5; Case 2: rules 5, 6, 7; Case 3: rule 5.]
3. The Equal Credit Opportunity Act prohibits creditors from requiring a spouse to cosign for individual, unsecured credit and, thus, be liable for the debt. Show Transparency 6, which illustrates the advantages and disadvantages of cosigning a loan or disclosing support payments. Under the Equal Credit Opportunity Act, a creditor can require a consumer to disclose alimony or child support payments that will be relied on for repayment.
4. The importance of having a good credit record and how consumers can protect their credit records are covered in Section 3—The Fair Credit Reporting Act. However, the Equal Credit Opportunity Act also contains provisions to protect the married woman from the "disappearing" credit history. Use (optional) Reading 2 to inform women of their right to separate credit histories and what to do if they have used or are using credit accounts opened prior to June 1977.

Topic 5—What If You're Denied Credit?

Objective: Student will know what information a creditor is required to give a rejected credit applicant. Student will know what steps to take to dispute adverse action taken on a credit application.

Materials Needed:
Flow Chart—"What If You're Denied Credit?"
"Statement of Credit Denial, Termination or Change"

Directions:

1. In addition to prohibiting creditors from asking certain questions or denying credit on the basis of prohibited information, the Equal Credit Opportunity Act requires creditors to reveal their reasons for denying credit. Consumers may then dispute a creditor's action and/or identify errors. If the reason for credit denial is valid, the consumer will know what to change in order to qualify for credit in the future (establish a credit record, increase income, pay off debts, etc.).
2. Distribute to students the flow chart "What If You're Denied Credit?" Use the chart to discuss what rights consumers have when they are denied credit and what action they can take. Ask students how they would know whether the reason given for denying credit is valid or invalid. For example, suppose you have lived in town one year, and a creditor gives you as the reason for denying credit, "too short a period of residence." Is that a valid reason or is there another, perhaps discriminatory, reason for the credit denial? [Without knowing a particular creditor's policies, a consumer cannot easily judge whether discrimination has occurred. An attorney or a federal agency can review—at the consumer's request—other files to see if the consumer has been treated differently from other applicants.]

3. Distribute to students copies of the Statement of Credit Denial, Termination or Change. Point out and discuss the following parts of the notice:
   (1) Description of adverse action taken (denial, termination, or change of credit terms).
   (2) Principal reason(s) for adverse action concerning credit. (If a creditor does not disclose the reason(s) for denial, you must be told you have the right to request the reason(s) within 60 days.)
   (3) Disclosure of use of information from an outside source. (See Section 3—The Fair Credit Reporting Act, Topic 2.)
   (4) Statement of rights under the Equal Credit Opportunity Act.
   (5) Name and address of the federal enforcement agency.

Topic 6—The Economics of the Equal Credit Opportunity Act

Objective: Student can identify how the Equal Credit Opportunity Act provides an economic incentive for creditors to evaluate credit applicants on the basis of their individual circumstances. Student is aware of the regulatory costs of the Equal Credit Opportunity Act and how these costs may affect creditors, credit users, and consumers in general.

Materials Needed:
Transparency 7—"A Delicate Balance"
Case Study 3

Directions:
1. The Equal Credit Opportunity Act distinguishes between (1) information creditors need to make good credit decisions and (2) information not related to credit applicants' creditworthiness that may negatively affect their chances of obtaining credit. Show Transparency 7, which illustrates how the law attempts to strike a balance between the needs of the creditor and the concerns of the consumer. Point out to students that in each of the situations listed, the balance reached is different. Some information cannot be asked for under any circumstances. Other information can be asked for in some instances, since it might reflect an individual's creditworthiness, but not in other instances. Some information can be asked for in every situation. Ask students if it would be feasible to eliminate all discrimination by limiting the amount of information a creditor may obtain. [Often sight alone will indicate the sex, race, or national origin of an applicant. There is no effective way of stopping creditors from receiving information in addition to what they receive on a written form.]

2. In order to prevent creditors from obtaining and using certain information about an applicant, legal penalties may be imposed if a creditor uses practices or actions that are found to be discriminatory. Use the questions below to examine how the Equal Credit Opportunity Act shifts the "costs" of credit denials from the victim who cannot change his/her race, religion, sex or marital status, age, etc., to a creditor who can avoid legal penalties through compliance with the law:

   a. Before the Equal Credit Opportunity Act, consumers denied credit for reasons not based on their ability and willingness to repay incurred all the "costs" of the credit decision. What were some of these costs? [Consumers were unable to enjoy the financial benefits of home ownership or other "investments," such as a college education. They could not use credit to take advantage of lower prices or to buy desired items now. If they used their savings to pay cash, they would lose their interest income. They could be denied access to some goods or services, such as hotel accommodations or rental cars, even if they could pay cash.]

   b. Before the Equal Credit Opportunity Act, creditors who denied credit for reasons that were not valid incurred few or no costs. Why not? [Even if creditors missed an opportunity to grant credit to an applicant who could repay, there would normally be someone else to whom they could extend credit. (Interest ceilings kept the demand high for credit that was relatively inexpensive.) Creditors would seldom lose any interest income as a result of denying someone credit. Also, creditors could base a decision to deny credit on any information they obtained about an applicant and not reveal the reason for denial. Thus, it was very difficult for a consumer to recognize or prove when credit was denied for a reason that was not valid.]

   c. Why do you think that before the Act some creditors would deny credit to all persons who were of a certain race, religion, nationality, sex, or marital status? [It may have been easier and cheaper for creditors to screen out "high-risk" applicants on a broad basis—for example, all divorced persons—than to analyze each individual's situation. And, as mentioned before, there always was someone else to whom they could extend credit.]

   d. How does the law prevent creditors from denying credit on the basis of the rate of default for all persons who are members of a certain race, religion, nationality, sex, marital status, etc., rather than on the basis of an individual's ability and willingness to repay? [Creditors now can incur legal penalties if they deny credit on the basis of information not related to an individual's creditworthiness. Thus, there is an economic incentive for a creditor to evaluate each credit applicant on an individual basis rather than to screen out all "high-risk" applicants.]

   e. Creditors can incur other costs as they comply with the provisions of the Equal Credit Opportunity Act. These regulatory or compliance costs, as they are called, include the costs of changes creditors had to make to ensure that their advertising, application, interviewing, evaluation, and notification procedures are legal. Do you think consumers are affected by the compliance costs incurred by creditors? If so, explain. [Yes. Everyone's taxes help pay the costs of any government regulation. In addition, consumers may pay higher prices for credit or, possibly, higher prices in general because of the compliance costs incurred by creditors. Or creditors may decide to supply less credit to consumers because of their increased costs. Consumers also may incur costs in the course of exercising their legal rights.]

3. Distribute Case Study 3 to students. This may be assigned to students individually or as a class. Students are to read each case and identify the "economic costs" to the creditor and the consumer of credit denial *before* (Case 1) and *after* (Case 2) passage of the Equal Credit Opportunity Act. When students have answered the questions following each case, go over their responses. [See "Answer Key."]

Answer Key

Pretest

1. *False.* The "three Cs of credit" refer to an applicant's "capacity to pay," "character," and "collateral" and are used by creditors to evaluate creditworthiness.
2. *True.* A creditor may require applicants for joint or secured credit to state whether they are "married," "unmarried," or "separated." A creditor may not ask unmarried applicants to reveal if they are single, divorced, or widowed.
3. *False.* A creditor may ask an applicant's age to establish that he/she can legally enter into a contract or determine how age may affect repayment.
4. *False.* Although creditors cannot deny credit solely on the basis of an applicant's age, sex, marital status, race, color, religion, or national origin, credit can be denied to anyone who is not creditworthy.
5. *False.* A creditor is required to tell consumers why credit was denied or that they have the right to request the reason within 60 days.
6. *False.* Alimony or child support payments need to be revealed only if a consumer will be relying on them to repay credit.
7. *True.* A creditor cannot deny credit on the basis of a person's age; however, the specific amount and repayment terms may be changed to protect the creditor against possible losses.
8. *False.* If a consumer is creditworthy, a creditor cannot deny credit because he/she has exercised rights under the federal consumer credit protection laws.
9. *True.* Creditworthy persons who may have been discouraged from applying for credit or denied credit because of their age, sex or marital status, race, religion, national origin, or source of income are now able to apply for and obtain credit.
10. *True.* Creditors may shift to consumers some or all of the additional costs incurred as a result of the Equal Credit Opportunity Act. These costs include possible legal costs as well as the costs of complying with the law.

Topic 1, Simulation, Direction 4

Applicant 1: (a) capacity to pay, character; (b) character; (c) capacity to pay; (d) not valid; (e) capacity to pay, collateral

Applicant 2: (a) capacity to pay; (b) not valid; (c) character; (d) collateral (also capacity to pay if mortgage payments are a large percentage of disposable income); (e) character, capacity to pay

Applicant 3: (a) not valid; (b) not valid; (c) character; (d) not valid; (e) not valid

Applicant 4: (a) not valid; (b) character; (c) capacity to pay, character; (d) capacity to pay, collateral; (e) not valid

Topic 3, Case Study 1

Case 1:

The bank probably decided to require a cosigner because of John's lack of employment and credit history and not because of his age. A young person often has not yet established creditworthiness. However, the law requires that a creditor evaluate each applicant on the basis of the individual circumstances. Credit cannot be denied solely on the basis of a person's age.

Case 2:

It appears that the Fernandos were denied credit because they were over 62 and living on retirement income. A creditor cannot legally deny credit because an applicant is not eligible for credit-life insurance or is no longer employed. If the Fernandos' income is less than the amount required for a "Supertraveler" credit card, however, the credit card company may legally deny them credit.

Case 3:

It appears that Mrs. Stone has been denied overdraft protection because she has reached age 62. A creditor cannot legally close or change the terms of a credit account or require a new application solely on the basis of a person's age. Only if it can be shown that Mrs. Stone, upon reaching age 62, is unable or unwilling to repay can she be denied credit. If Mrs. Stone had just reached retirement age, the credit option on her account could be terminated if her income was insufficient. However, the financial institution would be required to consider all reliable retirement income.

Topic 3, Transparency 4

Under the Equal Credit Opportunity Act, the age of an elderly applicant (62 years or older) must be scored at least as high as the age of any younger applicant. The credit-scoring system shown on Transparency 4 must be changed as shown below to comply with the law:

Age of Applicant	Points Assigned to Age By Credit-Scoring System
15-19 years	0
20-24 years	1
25-29 years	2
30-49 years	3
50-59 years	3
60-61 years	2
62 years and over	3

[An elderly person's age must be scored as high as the age of a person who is between the ages of 30 and 59.]

Topic 4, Case Study 2

Case 1:

Amy was denied an individual credit account with Good Value Stores solely because of her new marital status. This is prohibited by law. A married woman has the right to open and maintain a credit account in her own legal name (maiden name, husband's surname, or combined surname) as long as she is creditworthy.

Case 2:

By not considering Ms. Allison's alimony and child support payments, the bank may be treating her less favorably because of her marital status and source of income. All reliable sources of income must be considered by a creditor who is evaluating an applicant's ability to repay. The bank may require evidence that her earned income and payments received from a former spouse are reliable, and it may deny credit if her income is insufficient.

Case 3:

Without being given other facts, we cannot know if credit was denied legally or illegally. The legal test for discrimination is whether the women have been treated less favorably *because* of their sex or marital status. The sexist remark by the loan officer implies that they may have been denied credit on the basis of their sex. However, such a remark does not prove discrimination. If it could be shown that the bank had granted loans in similar circumstances for male-owned businesses, discrimination would be proved.

Topic 6, Case Study 3

Case 1:

1. Frank paid $1,000 more to buy the car with cash than he would have paid using credit. In addition, he may have lost interest and dividend income by converting "assets" to cash.
2. The bank incurred the cost of processing an application for a loan that was not granted.

Case 2:

1. Mr. Thompson spent time learning about his rights, writing to the creditor to learn the reason for credit denial, and arranging and attending a meeting at the bank. Mr. Thompson also had to pay his own transportation expenses.
2. The bank spent time notifying Mr. Thompson that credit was denied, responding to his request for the reason for denial, meeting with him, and processing his application a second time. The bank also paid the postage to notify him of its decision and the reason for its decision. Besides the costs specific to this transaction, the bank also incurs the cost of continually monitoring its procedures to ensure that they comply with the law.

Pretest

Directions: Circle "T" if the statement is true; circle "F" if the statement is false.

T F 1. The "three Cs of credit" used by creditors in deciding to grant or deny credit to a particular applicant are cost, conditions, and collateral.

T F 2. In certain situations a creditor may ask a credit applicant if he/she is married, unmarried, or separated.

T F 3. Because it is illegal to deny credit on the basis of age, a creditor may not request an applicant's date of birth.

T F 4. A person who is a member of a minority has the right to be granted credit by any creditor to whom he/she applies.

T F 5. Rejected credit applicants have no way of learning the actual reasons why they have been denied credit.

T F 6. A credit applicant must reveal to a potential creditor any alimony or child support payments received from a former spouse.

T F 7. A creditor may require a higher down payment or a shorter repayment period when extending credit to a person who is 62 years or older.

T F 8. A consumer who takes legal action against a creditor will probably be denied credit in the future by other creditors.

T F 9. The Equal Credit Opportunity Act may help people obtain credit who previously were denied credit.

T F 10. As a result of the Equal Credit Opportunity Act, consumers may pay higher prices for goods or services or higher interest rates on credit.

The 3 Cs of Credit

Capacity Can You Repay the Debt?

Occupation? Place of employment? How reliable is your income? Salary? Do you have any other sources of income?	**Income**
Number of dependents? Do you pay alimony or child support? Current debts?	**Expenses**

Character Will You Repay the Debt?

Have you used credit before? For what purpose have you used credit? Do you pay your bills on time? Do you live within your means?	**Credit History**
How long have you lived at your present address? Do you own your home? How long have you been employed by your present employer?	**Stability**

Collateral What If You Don't Repay the Debt?

What assets do you have to secure the loan — car, home, furniture?
What sources do you have for repaying debt besides income — savings, stocks, bonds, insurance?

Who's a Good Credit Risk?

Directions: Each applicant described below has applied for a $4,000 loan to purchase a more fuel-efficient automobile. Imagine you are loan officers at a financial institution, and you must decide whether to approve or deny loans for each of the four applicants. You have been given five pieces of information about each applicant. Using this information, evaluate each applicant's ability and willingness to repay and make the "best" decision you can.

Applicant 1

a. "Has ten charge accounts"
b. "Address has not changed for five years"
c. "Has six children"
d. "62 years old"
e. "Owns stock"

Action Taken on Loan Application:

Approved Denied (circle one)

Reason for Action Taken:

Applicant 3

a. "Receives public assistance payments"
b. "Divorced"
c. "Pays bills on time"
d. "Works part-time"
e. "Female"

Action Taken on Loan Application:

Approved Rejected (circle one)

Reason for Action Taken:

Applicant 2

a. "Annual income of $25,000"
b. "Caucasian"
c. "Installment loan payments are delinquent"
d. "Owns or is buying a home"
e. "Has an overdrawn checking account"

Action Taken on Loan Application:

Approved Rejected (circle one)

Reason for Action Taken:

Applicant 4

a. "21 years old"
b. "Has no credit history"
c. "Has been on present job for 10 months"
d. "Has a savings account"
e. "Mexican-American"

Action Taken on Loan Application:

Approved Rejected (circle one)

Reason for Action Taken:

Your Equal Credit Opportunity Rights

A creditor is prohibited from discriminating against you on the basis of:

- age;
- sex or marital status;
- race, color, religion, or natural origin;
- reliance on income from a public assistance program;
- a "good faith" exercise of your rights under the federal consumer credit protection laws.

A creditor cannot discourage you from applying for credit if you are a reasonable applicant.

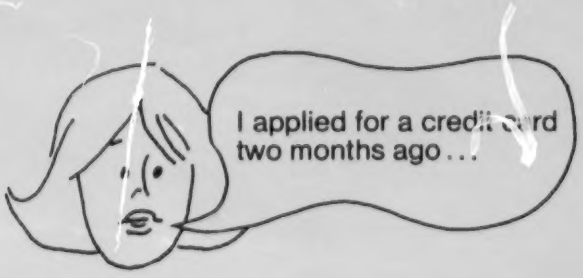
The application form must only ask for information permitted by law. A creditor cannot ask:

- your sex;*
- your race, color, religion, or national origin (may ask immigration status);*
- about your birth control practices or your capability or intention to have children;
- your marital status in applications for unsecured, individual credit;
- information about a spouse or former spouse except in certain situations.

*This information must be asked for monitoring purposes in real estate credit.

In evaluating your application, creditors:

- cannot ignore income derived from a public assistance program, retirement income, or part-time employment.
- cannot consider aggregate statistics about the likelihood of certain groups bearing or rearing children.
- cannot automatically deny credit because you are an elderly person.
- must consider credit history of accounts that you have used or are liable for, if they customarily review credit histories.

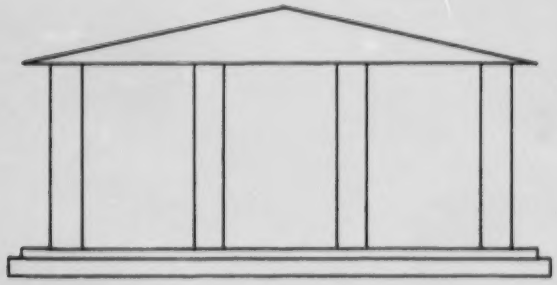


If a creditor denies you credit, he/she must notify you within 30 days and provide:

- a statement of reasons for the denial of credit (or inform you of your right to receive such a statement).
- an explanation of the Equal Credit Opportunity Act.
- the name and address of the agency which enforces the Act.

If a creditor grants you credit, he/she:

- must allow you credit in your own name (including birth-given or combined surname).
- cannot require a spouse to cosign the note.
- must keep joint account records which show that both spouses use credit or have cosigned the note.



If you believe the creditor has denied you credit illegally, or has otherwise violated the law, you may:

- notify the federal agency which supervises the creditor.
- sue for actual and punitive damages (including attorney's fees and costs).*

*Up to $10,000 in an individual action, or the lesser of $500,000 or 1% of the creditor's net worth in a class action.

Credit Application

Section A—Information Regarding Applicant

Full Name (Last, First, Middle): _____ Birthdate: / /

Present Street Address: _____ Years there: _____

City: _____ State: _____ Zip: _____

Social Security No.: _____ Driver's License No.: _____

Previous Street Address: _____ Years there: _____

City: _____ State: _____ Zip: _____

Present Employer: _____ Years there: _____ Telephone: _____

Position or title: _____ Name of supervisor: _____

Employer's Address: _____

Previous Employer: _____ Years there: _____

Previous Employer's Address: _____

Present net salary or commission: $_____ per _____. No. Dependents: _____ Ages: _____

Alimony, child support, or separate maintenance income need not be revealed if you do not wish to have it considered as a basis for repaying this obligation.

Alimony, child support, separate maintenance received under:

court order ☐ written agreement ☐ oral understanding ☐

Other income: $_____ per _____. Source(s) of other income: _____

Is any income listed in this Section likely to be reduced in the next two years?

☐ Yes (Explain in detail on a separate sheet.) No ☐

Have you ever received credit from us? _____ When? _____ Office: _____

Checking Account No.: _____ Institution and Branch: _____

Savings Account No.: _____ Institution and Branch: _____

Name of nearest relative not living with you: _____ Telephone: _____

Relationship: _____ Address: _____

Section B—Information Regarding Joint Applicant, User, or Other Party

(Same information as requested for Applicant in Section A.)

Section C—Marital Status

(Do not complete if this is an application for an individual account.)

Applicant: ☐ Married ☐ Separated ☐ Unmarried (including single, divorced, and widowed)

Other Party: ☐ Married ☐ Separated ☐ Unmarried (including single, divorced, and widowed)

Section D—Asset and Debt Information

Case Study 1

Case 1:
John Jones, a recent college graduate, has accepted a teaching position at Greenstown High School. John moves to Greenstown and applies for a car loan at a local bank. He has never used credit or obtained a loan. The bank notifies him that it will not approve the loan unless he has a cosigner.

Has the bank denied credit on the basis of John's age?

Case 2:
Mr. and Mrs. Fernando were both employed for over 40 years. They have recently retired and have a retirement income consisting of pensions, social security, and interest income. The Fernandos want a "Supertraveler" credit card to use when they travel to Acapulco next year, and they apply at the local Supertraveler office. Their credit application is rejected because, they are told, they are not employed and are ineligible for credit-life insurance. (Credit-life insurance repays credit if the borrower dies.)

Has the credit card company denied credit on the basis of Mr. and Mrs. Fernando's age?

Case 3:
Mrs. Stone received a letter from her financial institution which included the following statement:

> When you opened your account, we explained why it was necessary to restrict the "check-credit" account to persons under 62 years of age. Our records indicate you have now reached age 62. We must ask that you stop writing checks immediately.

The letter continued, stating Mrs. Stone could open a new transaction account, however, without the "line of credit."

Has the financial institution denied credit on the basis of Mrs. Stone's age?

Credit and Age

A Creditor Cannot:

1. Deny credit because you have reached a certain age.
2. Deny credit because you are not employed if you have adequate pension or other retirement income.
3. Deny credit because you are not eligible for credit-life insurance.
4. Close or change an account, or require you to reapply because you have reached a certain age or have retired.

A Creditor Can:

5. Close or change an account, or require you to reapply, if there's evidence you are unwilling or unable to repay.
6. Require more collateral, a larger down payment, or a shorter repayment period on a loan if you are an elderly person.

Scoring Age*

Credit Applicant's Age	Number of Points Assigned to Applicant's Age
15-19 yrs.	0
20-24 yrs.	1
25-29 yrs.	2
30-49 yrs.	3
50-59 yrs.	3
60-64 yrs.	2
65 yrs. and over	1

*A hypothetical "scoring" of age in a credit-scoring system prior to the Equal Credit Opportunity Act.

Case Study 2

Case 1

Amy Sweet recently married. Amy has been employed for the past five years at the same company. She plans to continue working.

Amy is notified by Good Value Stores that her individual credit account, which she opened three years ago, will be closed. She is told that she and her husband must reapply for credit because Good Value requires all married persons to have a joint account.

Did Good Value deny credit on the basis of Ms. Sweet's sex or marital status?

Case 2

Joyce Allison is divorced and has two young children. She takes care of her children during the day and works evenings as a waitress. Ms. Allison also receives alimony and child support from her former husband.

She applies for a car loan at her bank, but her application is rejected. The bank will only consider earned income, not alimony or child support payments. Joyce's income as a waitress is "insufficient" for her to qualify for the loan, so she is denied credit.

Did the bank deny credit on the basis of Ms. Allison's marital status or source of income?

Case 3

Mary McGurran and Maria Garcia own and operate a construction company which specializes in remodeling older homes. Both are in their late twenties and unmarried. They have run the company successfully for seven years and have received several loans guaranteed by the Small Business Administration. When they call on their bank about a loan to construct a new headquarters, the banker balks. Mr. Brink, the loan officer, says that without the SBA guarantee, the bank would never "take a chance on two little girls fixing up houses in their spare time." The vice-president of the bank apologizes for Mr. Brink's comment, but the loan is denied.

Did the bank deny credit on the basis of Ms. McGurran's and Ms. Garcia's sex or marital status?

Credit Rights of Women

A Creditor Cannot:

1. Refuse you individual credit in your own name.
2. Require a spouse to cosign a loan. Any creditworthy person can be your cosigner if one is required.
3. Ask about your birth control practices or family plans or assume income will be interrupted to have children.
4. Consider whether you have a telephone listing in your own name.

A Creditor Must:

5. Evaluate you on the same basis as applicants who are male or who have a different marital status.
6. Consider income from part-time employment.
7. Consider reliable alimony, child support, or separate maintenance payments.
8. Consider payment history on all joint accounts which accurately reflects your credit history.
9. Report payment history on an account if you use the account jointly with your spouse.
10. Disregard information on accounts if you can prove it does not reflect your ability or willingness to repay.

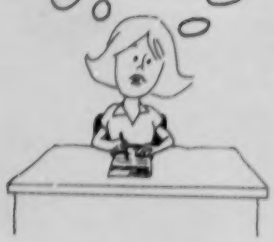
Freedom of Choice

They'll know I'm divorced . . .

Approval may depend on how reliable the payments are . . .

My income will be higher . . .

It may help me qualify for credit . . .



Should I Reveal Child Support Payments?

It'll help me establish a credit record . . .

It may help me obtain credit in my own name . . .

I'll be liable for the debt . . .

Failure to repay may damage my credit record . . .

Should I Cosign His Loan?

The Problem of the Disappearing Credit History

In Section 1, we saw that establishing a good credit history is very important to the creditors to whom you apply. The Equal Credit Opportunity Act was passed partly because credit history was collected and reported differently for married women and men. Many credit bureaus would routinely collect information on the use of joint accounts in the husband's name only. As long as the couple remained married, and the woman did not want separate credit, this practice usually did not present problems. If the man died, however, the woman would find that she had no credit history, despite years of good bill-paying habits. If the couple divorced, the man would retain the credit history which they established together, and the woman would be forced to start again building a good credit record. When a woman who was married, widowed, or divorced applied for individual credit based on her own assets and income, she would appear to have no credit history. The Equal Credit Opportunity Act addressed this problem of the "disappearing" credit history.

The easiest solution to this problem was for creditors to report information on joint credit accounts to credit bureaus in the names of both spouses. Credit bureaus would then establish separate credit records for each spouse. Beginning on June 1, 1977, creditors and credit bureaus were required by law and regulation to establish these procedures. Over time, therefore, the system should be corrected to accurately reflect the credit use for each spouse.

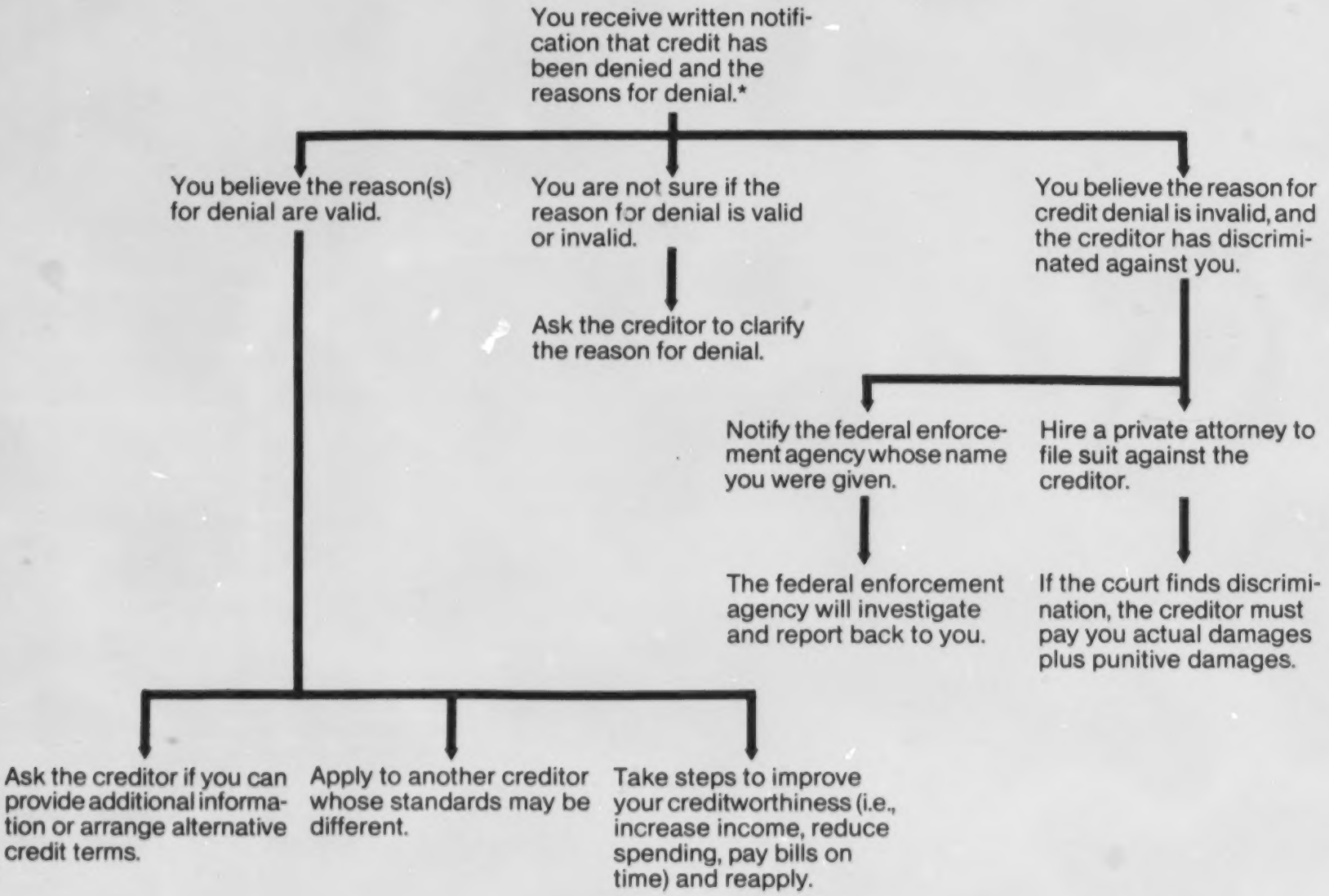
However, many women continue to use joint accounts issued before June 1977, and continue to pay on loans existing before June 1977. In order to ensure that the credit history on these accounts is not lost, those women probably need to take some affirmative action. The first step is for a woman simply to review information currently on file at her local credit bureau to determine the extent of the problem. If her credit history is incomplete, she should:

1. Contact creditors not included in her file and ask that they begin reporting information in both spouses' names, or
2. Tell the credit bureau that the file is incomplete and provide them with names of the missing creditors.

These steps should be taken *prior* to the time a woman applies for credit in her own name. When a woman does apply for credit, the creditor must look at all accounts or loans she has used or has cosigned, if the information is available. If requested, the creditor may disregard bad accounts which appear in a woman's credit history if she can show she never used or was not responsible for these accounts. A woman can also request that a creditor consider an account which doesn't appear in her credit history, if she can prove it accurately reflects her creditworthiness.

Consumers who have yet to establish credit will now automatically be given the credit history for accounts which they and their spouses will use or for which they will be liable. This protection is very recent, however. Other consumers may need to take specific action to ensure that their credit histories accurately reflect their use of credit.

What If You're Denied Credit?


You receive written notification that credit has been denied and the reasons for denial.*
You believe the reason(s) for denial are valid.
You are not sure if the reason for denial is valid or invalid.
You believe the reason for credit denial is invalid, and the creditor has discriminated against you.
Ask the creditor to clarify the reason for denial.
Notify the federal enforcement agency whose name you were given.
Hire a private attorney to file suit against the creditor.
The federal enforcement agency will investigate and report back to you.
If the court finds discrimination, the creditor must pay you actual damages plus punitive damages.
Ask the creditor if you can provide additional information or arrange alternative credit terms.
Apply to another creditor whose standards may be different.
Take steps to improve your creditworthiness (i.e., increase income, reduce spending, pay bills on time) and reapply.

*If a creditor receives no more than 150 applications during a calendar year, the disclosures may be oral.

EMPLOYEES' CREDIT UNION

123 Elm Street
Goodtown, U.S.A.
876-5432

Statement of Credit Denial, Termination or Change

Date

Applicant's Name	Address
John C. Borrower	452 Main Street

Description of account, transaction or requested credit:
Automobile Loan

1 Description of adverse action taken:
Denied

Principal Reason(s) for Adverse Action Concerning Credit

2
- ☐ Credit application incomplete.
- ☐ Insufficient credit references.
- ☐ Unable to verify credit references.
- ☐ Length of employment
- ☐ Temporary or irregular employment.
- ☐ Unable to verify employment.
- ☒ Insufficient income.
- ☐ Excessive obligations.
- ☐ Unable to verify income.
- ☐ Too short a period of residence.
- ☐ Temporary residence.
- ☐ Other specify .....
- ☐ Unable to verify residence.
- ☐ No credit file.
- ☐ Insufficient credit file.
- ☐ Delinquent credit obligations.
- ☐ Garnishment, attachment, foreclosure, repossession, or suit.
- ☐ Bankruptcy.
- ☐ Inadequate collateral
- ☐ We do not grant credit to any applicant on the terms and conditions you request.

3 Disclosure of Use of Information Obtained From an Outside Source

☒ Disclosure inapplicable.

☐ Information obtained in a report from a consumer reporting agency

Name: _____

Address: _____

Phone: _____

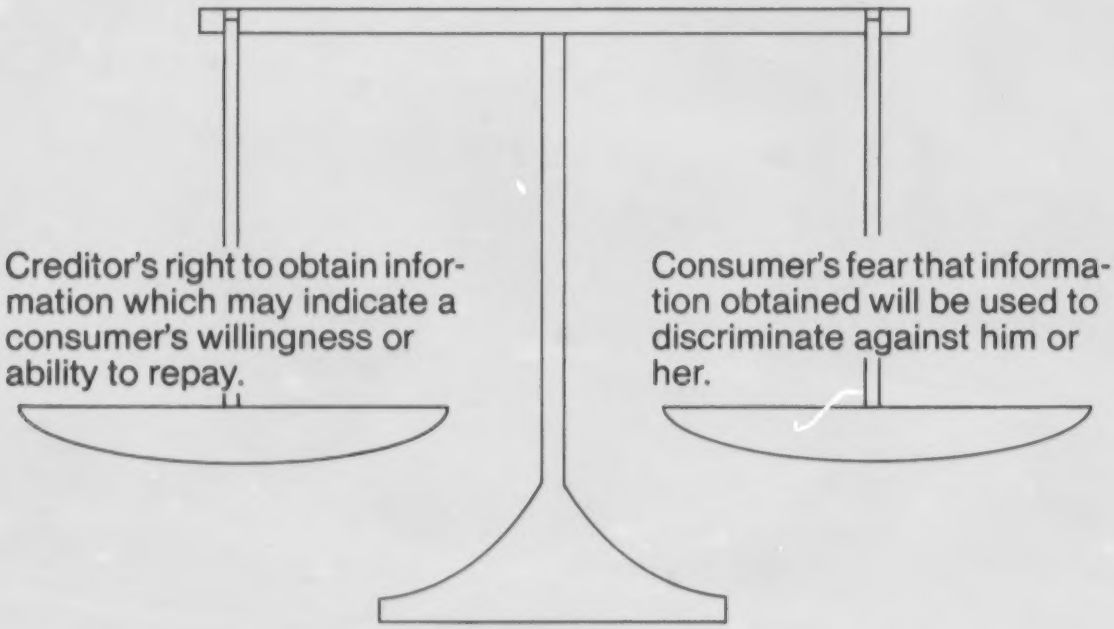
☐ Information obtained from an outside source other than a consumer reporting agency. Under the Fair Credit Reporting Act, you have the right to make a written request, within 60 days of receipt of this notice, for disclosure of the nature of the adverse information.

4 The Federal Equal Credit Opportunity Act prohibit creditors from discriminating against credit applicants on the basis of race, color, religion, national origin, sex, marital status, age (providing that the applicant has the capacity to enter into a binding contract); because all or part of the applicant's income derives from any public assistance program; or because the applicant has in good faith exercised any right under the Consumer Credit Protection Act. The Federal Agency that administors compliance with this law concerning this creditor is the Federal Trade Commission, 55 East Monroe Street, Suite 1437, Chicago, Illinois 60603.

5

55

A Delicate Balance


Creditor's right to obtain information which may indicate a consumer's willingness or ability to repay.
Consumer's fear that information obtained will be used to discriminate against him or her.

Under the Equal Credit Opportunity Act . . .

- A creditor cannot ask a person's race, religion, sex, or national origin.
- A creditor can ask a person's marital status in some instances and can always ask the number of dependents.
- A consumer has the option to disclose monies received from alimony or child support.
- A creditor can always ask an applicant's age.

Case Study 3

Case 1: Before the Equal Credit Opportunity Act

Frank Thompson, a retired businessman, decided to purchase a new car on sale for $9,000. He applied for a loan at his local bank. Three weeks later he was notified that his application had been rejected. He called the bank to find out why his loan application was not approved and was told he did not qualify for the loan.

Frank applied to another creditor and again was turned down. At this point, he sold some shares of stock and cashed in some bonds so he could pay cash for the car. Since he had first applied for a loan, the sale price was no longer good, and he had to pay $10,000.

1. What costs did Mr. Thompson incur as a result of being denied credit?

2. Assuming Mr. Thompson would have repaid the loan, what costs did the bank incur as a result of denying him credit?

Case 2: After the Equal Credit Opportunity Act

Frank Thompson applied for an automobile loan at his bank. He planned to purchase a $9,000 car with a down payment of $1,500. Ten days after he submitted his application, he was notified in writing that the loan was not approved. The notice included a statement of his rights under the Equal Credit Opportunity Act. Exercising those rights, Frank wrote to the bank requesting the reason for his being denied credit.

The bank answered his letter promptly telling him that he had not been granted the loan because of "insufficient income." Frank questioned this because, in addition to his pension, he received social security payments and interest and dividend income. He called the bank to arrange a meeting to discuss the situation. That week he met with the loan officer and presented evidence of his additional income. The loan officer realized the bank had not considered all his income sources. He would qualify for a loan; however, they would require a larger down payment—$2,500—to reduce the monthly payment amount.

1. What costs did Mr. Thompson incur by exercising his rights under the Equal Opportunity Act?

2. What costs did the bank incur in complying with the provisions of the Equal Credit Opportunity Act?

YOUR CREDIT RIGHTS

SECTION 3

The Fair Credit Reporting Act

Introduction

Until 1969, credit reporting was very much a "mystery" to most consumers. Some consumers were unaware that reports on their bill-paying habits even existed. Even if they did know, they could only guess at what information was in such a report. For the majority of consumers who had accurate and favorable credit reports, this wasn't a problem. But for a significant number of persons, the information was wrong and could result in being denied credit—or even employment! In this section, students will learn what a credit report is and how creditors use the information contained in reports to make credit decisions. Using case studies, readings, and flow charts, students will learn what to do if they believe credit has been denied on the basis of an inaccurate credit report.

Key Concepts

1. Credit bureaus collect personal and employment data on consumers and maintain records of how consumers use and repay credit.
2. Credit bureaus and investigative agencies provide up-to-date information needed by creditors, employers, and insurers to make sound business decisions.
3. Consumers who are denied credit on the basis of information contained in a credit report must be told the name and address of the credit bureau which provided the information.
4. Upon request, credit bureaus must tell consumers the general substance and nature of information contained in their credit files.
5. Consumers have the right to dispute information in their credit reports. Credit bureaus must reinvestigate disputed information, delete information that cannot be verified, and correct errors.

Topic 1—Understanding Your Credit Report

Objective: Student will know why credit bureaus exist and how they benefit both creditors and consumers. In a simulation, students will make "credit decisions" based on information in a credit report.

Materials Needed:

Reading 1—"What Is a Credit Bureau?"
Sample Credit Report
"Understanding Your Credit Report"
Transparency 1—"Manner of Payment"
Simulation—"Would You Grant Credit?"

Directions:

1. Write "credit bureau" on the chalkboard. Ask students if they know what a credit bureau is and what it does. Write their responses on the chalkboard or poster paper. (This exercise may reveal misconceptions students have about the functions of credit bureaus.)
2. Distribute and assign Reading 1. Discuss the reading, ensuring that students can answer correctly the questions posed at the beginning of each paragraph. Define and discuss the terms "credit file," "credit report," "credit record," "credit rating," etc., as needed.
3. Distribute the sample credit report and "Understanding Your Credit Report" to students. As a class, interpret the information in Mr. Consumer's report using the explanations for various sections of the credit report.
4. Using Transparency 1, explain how individual credit accounts are "rated" by credit bureaus. Stress that this rating is based only on data received from creditors who have had actual experiences with borrowers. These numerical ratings do not individually, or in combination, represent a consumer's credit rating. Users of credit reports may or may not assign to a consumer a credit rating based on information obtained from a credit report as well as other sources.
5. Using the sample credit report and "Understanding Your Credit Report," conduct the simulation as follows. Divide the class into small groups of four to five students, giving each group the simulation, "Would You Grant Credit?" As a class, read the simulation directions. You may want to review with students the "3 Cs of Credit" (Section 2, Topic 1, Transparency 1) before they make their credit decisions. Tell stu-

dents you will ask each group later what its decision was and what information in the credit report influenced its decision.

(Note: It's possible that groups or students within a group will not agree on whether Mr. Consumer should be granted credit. Such disagreement reflects what may happen in real-life situations. The credit granting standards of different creditors vary. An applicant may indeed be granted credit by one creditor and denied credit by another.)

Topic 2—The Fair Credit Reporting Act

Objective: Student will know how a consumer can learn what information creditors, employers, and insurers receive from a credit bureau and how credit report errors can be corrected. Student will know when "adverse" information must be deleted from a consumer's credit file.

Materials Needed:
Reading 2—"Consumers Testify on Credit Report Errors"
Reading 3—"Your Fair Credit Reporting Rights"
Transparency 2—"Who Has the Stronger Interest?"

Directions:

1. In Sections 1 and 2, students learned how important it is for a consumer to establish credit in his/her own name. It is equally important that the agencies collecting and maintaining credit and other data have accurate information. As credit use increased and the credit process became computerized, the potential for credit reporting errors also increased. Assign students all or part of Reading 2 which is based on testimony concerning alleged credit and employment problems of a few consumers prior to 1968. Ask individual students to identify specific problems the consumers testifying had experienced as a result of not being able to verify or dispute credit information.

2. The Fair Credit Reporting Act, passed by Congress in 1968, gave consumers the right to know what specific information credit bureaus were providing to potential creditors, employers, and insurers. Under the Fair Credit Reporting Act, if credit is denied on the basis of information in a credit report, the applicant has to be told the name, address, and phone number of the credit bureau providing the information. Give each student Reading 3, which summarizes the provisions of the Act. As a class, read and discuss the rights and responsibilities of consumers, credit bureaus, and report users.

3. Show Transparency 2. This transparency deals with the issue of a consumer's right to "start over" after having had credit problems. The Fair Credit Reporting Act allows most adverse information to remain in a person's file for only seven years. Point out to students, however, that even seven years is a long time to have it recorded that you failed to pay a bill!

Vocabulary

Adverse Information	Information in a credit report which indicates a consumer may be unable or unwilling to repay credit.
Bankruptcy	A legal action in which most of a consumer's debts are discharged and assets (except for certain protected assets) are divided among creditors.
Credit Bureau	A firm which collects and provides to creditors, employers, and insurers information on how consumers use credit as well as other personal and financial data.
Credit File	All the information a consumer reporting agency has in its records on a particular consumer.
Credit Rating	A consumer's relative creditworthiness as determined by a creditor based on information obtained from the credit report, credit application, and interview.
Credit Report	A written, oral, or other communication from a credit bureau to a creditor, employer, or insurer concerning a consumer's credit history.
Consumer Reporting Agency	Any firm which regularly collects and provides to others information on consumers' bill-paying habits including credit bureaus, investigative agencies and some creditors.
Investigative Report	A report on a consumer which contains information on the individual's character, reputation, personal habits, and life-style obtained through interviews with neighbors, friends, and associates.
Investigative Reporting Agency	A firm which regularly collects and provides to others information on a consumer's character, reputation, personal habits, and life-style.
Outside Source	Any person or organization which provides information to a creditor on a consumer but is not a credit bureau or investigative reporting agency; e.g., a department store reporting its own experience to another creditor.
Statement of Dispute	A statement included in a credit or investigative report in which a consumer explains why he/she believes information in a report is inaccurate.
Valid Business Purpose	A credit, employment, insurance, or licensing decision or other bona fide reason for needing information contained in a credit report.

Topic 3—Correcting Credit Report Errors

Objective: Student will know how consumers can learn what information is in their credit files. In a role-playing activity, students take steps to verify and correct credit report information.

Materials Needed:
Flow Chart 1—"What If Your Credit Report Is Wrong?"
Case Study

Directions:

1. To help ensure the accuracy of credit reports, the Fair Credit Reporting Act gives consumers the right to know what information is in their credit reports. A consumer may check to see if information is correct at any time, but a credit bureau may charge a fee for this service. If a consumer is denied credit on the basis of information in a credit report, he/she may check to see if the information is accurate. Under these circumstances, a credit bureau cannot charge a consumer for revealing the contents of a report. Distribute Flow Chart 1 to students. As a class, read and discuss what a consumer may do if he/she is denied credit on the basis of information in a credit report.

2. Assign students the Case Study. Individually, or in groups, ask students to read each case and answer the questions that follow about the consumer's credit rights. When students have finished the assignment, discuss their responses. [See "Answer Key."]

3. Write the following role descriptions on the chalkboard and select students to assume each of the roles listed:
   Hand-Crafted Furniture, creditor
   John Jacobson, consumer
   Mrs. Green, interviewer for Small Town Credit Bureau
   Credit Manager, All Goods Department Store

   Explain the situation to students:

   "John Jacobson applied for credit at Hand-Crafted Furniture. His application was rejected because of adverse information in a credit report provided by Small Town Credit Bureau. He doesn't know what information in his credit report could justify the action, so he arranges to have an interview at the Small Town Credit Bureau. Mrs. Green, the interviewer, tells him his file indicates that a television set was repossessed by All Goods Department Store. Mr. Jacobson explains that he did purchase a television at All Goods, but he paid cash."

   Ask the students who will play the roles of the creditor, consumer, credit bureau interviewer, and credit manager to interact in an attempt to solve Mr. Jacobson's credit problem. Other students will be "observers." Ask the observers to make a list of the steps taken by each of the parties involved to resolve the problem. [See "Answer Key."]

4. As a follow-up to the role play, ask "observers" to list on the chalkboard each step taken by the role players to solve Mr. Jacobson's problem. Then ask the observers to evaluate how Mr. Jacobson, the credit bureau, and the creditors handled the situation. (Did anyone fail to do something he/she should have done? Did anyone violate the law?) [Refer to Topic 2, Reading 3—"Your Fair Credit Reporting Rights."]

Topic 4—What Is an Investigative Report?

Objective: Student will know what types of information are collected by investigative reporting agencies and the sources of their information. Student will be able to identify the special protections consumers have under the Fair Credit Reporting Act when an investigative report is ordered by a creditor, employer, or insurer.

Materials Needed:
Reading 4—"Charlie Green and the Mysterious Report"
Reading 5—"Investigative Reporting"
Transparency 3—"I'm Just Making a Credit Check"
Flow Chart 2—"What If an Investigative Report Is Ordered?

Directions:

1. Distribute and assign students Reading 4 and the questions that follow the reading. When they have completed the assignment, discuss students' answers and Charlie Green's alleged experiences as a result of the inaccurate investigative consumer report. [See "Answer Key."]

2. Assign students Reading 5, which explains what investigative agencies do and the special rules regarding the gathering of investigative information. Discuss the reading using the following questions:

   a. Do you think the possibility of making reporting errors is greater for a credit bureau or an investigative agency? Explain. [The possibility of inaccurate reporting is probably greater for an investigative agency than a credit bureau. Its information is obtained, in part, by conducting interviews and may be based on people's opinions or judgments about an applicant. Information on personal habits and life-styles is often difficult to verify or prove wrong. Credit bureaus, on the other hand, rely on public record information and data routinely obtained from creditors' payment records, which are easier to verify.]

   b. Do you think investigative agencies should reveal the names of persons providing information for an investigative report? [Student's opinions may vary on this question. Some sources may be reluctant to give adverse information if their identities will not remain confidential. On the other hand, if people know that sources will be identified, they may be discouraged from giving false or biased information, and the overall reliability of investigative-type information might improve.]

   (Note: The Fair Credit Reporting Act does not require investigative agencies to reveal the names of their sources.)

3. Show Transparency 3. The cartoon raises the question of whether investigative reporting constitutes an invasion of a consumer's privacy. As a class, discuss the questions listed on the transparency. [See "Answer Key."]

4. Distribute Flow Chart 2 listing the rights and responsibilities of (1) investigative agencies, (2) creditors, employers, and insurers who use investigative reports, and (3) consumers who are the subjects of such reports. Emphasize that consumers can prevent such investigations from being made by withdrawing their applications for credit, insurance, or employment.

Topic 5—The Economics of the Fair Credit Reporting Act

Objective: Student can identify the economic costs to credit bureaus and creditors of inaccurate credit reports and explain how they provide incentives for fair and accurate reporting. Student will be aware of the compliance costs of the Fair Credit Reporting Act and can state how these costs may be shifted to credit report users and consumers.

Materials Needed:
Transparency 4—"Confidential but Accessible"
Transparency 5—"Shifting Regulatory Costs"

Directions:

1. Before passage of the Fair Credit Reporting Act, credit and investigative information was considered strictly "confidential" and consumers could not learn the nature and substance of such information. An individual or a firm, however, could legally obtain a consumer's report even if the information was not needed for a legitimate business purpose. Under the Act, consumers not only are protected against unauthorized use of information, but they may learn the contents of reports provided to potential creditors, employers, and insurers. Use Transparency 4 to discuss how the Fair Credit Reporting Act provides for both the confidentiality and accessibility of consumer information.

2. Prior to the Act, errors in credit and investigative reports usually were not identified, and, thus, were seldom corrected. Because of this, reporting agencies incurred no additional costs when they provided inaccurate or incomplete information to creditors, employers, or insurers. The consumer, however, who is denied credit, employment, or insurance because of an erroneous report may incur actual, and possibly, psychological costs (embarrassment, frustration, inconvenience). Users of consumer reporting services also may incur costs as the result of using inaccurate information to make important business decisions. Use the questions below to discuss how the Fair Credit Reporting Act (1) "shifts" some of these direct costs to the reporting agencies which prepare reports and (2) provides economic incentives for fair and accurate consumer reporting:

   a. What direct costs does a credit bureau now incur if information provided to a creditor on a consumer is inaccurate? [If a consumer is denied credit on the basis of the erroneous information, he/she may ask the credit bureau to reveal the contents of the credit report. This costs the credit bureau time and money (wages). In addition, the credit bureau must reinvestigate, correct, or delete such information, and send updated reports to creditors who have received reports during the past six months. All of these activities increase the credit bureau's costs of doing business and may decrease its earnings. In addition, a credit bureau may be sued and incur legal penalties if it fails to comply with any of the provisions of the Fair Credit Reporting Act.]

   b. How can reporting agencies "avoid the potential costs of inaccurate reports? [The administrative costs of erroneous reports may be avoided or reduced by taking steps to ensure that reports are accurate: thoroughly investigating and verifying information, emphasizing the importance of preparing accurate reports, and having a well-trained staff. Legal penalties can be avoided by complying fully with the provisions of the Fair Credit Reporting Act; e.g, responding to consumer requests for information.]

   c. What direct costs does a creditor incur when a decision to grant or deny credit is made on the basis of an inaccurate credit report? [The decision may be wrong, and the creditor may not be repaid, or he/she may deny credit to a creditworthy applicant. The creditor may also incur the administrative costs of notifying the consumer of the name of the credit bureau and of his/her rights to learn the contents of the report, processing an application that later is rejected because of inaccurate information in a credit report, and processing an application a second time after an updated or corrected report is received.]

   d. Prior to the Act, neither creditors nor consumers knew when a credit report contained errors or was incomplete. Explain how consumers having access to the information in their reports and creditors receiving corrected reports help encourage fair and accurate credit reporting. [Creditors may learn that information "purchased" from a reporting agency was wrong or incomplete. Because they, too, may incur administrative and other costs as a result of erroneous reports, creditors might not want to use the services of a credit bureau that does not provide accurate and complete information. Consequently, credit bureaus risk losing business if consumer information is disputed and found to be in error too often.]

3. Ask students to list some "compliance costs" incurred by credit bureaus, investigative agencies, creditors, and other users of consumer reporting services as a result of the Fair Credit Reporting Act. (Explain that compliance, or regulatory, costs are incurred whether or not credit reports are accurate. They are unavoidable costs of doing business.) [Credit bureaus may have to reinvestigate disputed information that is "true." They also may have to help consumers write "statements of dispute" and include them in future reports. Investigative agencies may have to provide additional information about investigations. Creditors must provide the names, etc., of credit bureaus to consumers who are denied credit because of information in a credit report. Creditors, employers, and insurers must notify consumers when an investigative report is ordered and inform them of their right to learn more about the investigation.]

4. The costs of government regulation of credit and investigative reporting are not necessarily borne only by the reporting agencies and users of reporting services. Administrative costs and legal costs incurred by complying with the law and by consumers exercising their legal rights may be "shifted" to another party. Use Transparency 5 to discuss how credit bureaus and investigative agencies may shift costs to creditors who, in turn, may shift costs to consumers.

   (Note: In Topics 2-4 of this section, students learned about their rights with regard to consumer reporting and how to exercise these rights. This topic attempts to show students that these protections are not "free." There are costs associated with exercising one's rights under the Act—transportation, time away from work, seeking legal advice—as well as regulatory costs which may be passed on to consumers in the form of increased credit costs, higher prices, or the reduced availability of credit.)

Answer Key

Pretest

1. *False.* Credit bureaus are private firms which collect and distribute to their customers information on how consumers use credit as well as other financial data.
2. *False.* A credit report contains data on the actual experiences of creditors with a particular consumer—the type and amount of credit used and the payment history of the account. (Have bills been paid on time? Has a loan been repaid as agreed?)
3. *False.* Credit bureaus only provide data on a consumer's capacity to pay, collateral, and bill-paying habits. They do not rate a consumer as a good or bad credit risk.
4. *True.* Although credit reports contain only financial and public record information, investigative consumer reports may include information about a person's habits and life-styles obtained through interviews with neighbors and associates.
5. *False.* Only a person or organization making a credit, employment, or insurance decision or needing information for another valid business purpose may obtain a consumer's credit report.
6. *True.* Creditors, employees, and insurers have the right to order and use investigative reports to evaluate applicants. If they wish, to prevent such reports from being made, consumers can withdraw applications for credit, employment, or insurance.
7. *False.* Consumers are given a chance to "start over." Adverse information contained in a credit report must be deleted after seven years. Bankruptcy information, however, can be reported for 10 years.
8. *False.* Consumers can arrange with credit bureaus to learn the contents of their credit files. If they have been denied credit, consumers must receive this information free of charge.
9. *False.* If a consumer believes his/her credit report contains an error, it is the credit bureau's responsibility to reinvestigate the disputed information. If the bureau cannot verify the information, the bureau must delete it.
10. *True.* Creditors can reduce losses due to consumers not paying by granting credit only to persons who are good credit risks. This keeps down the cost of credit to consumers. Also, creditworthy persons may be granted credit in a more timely manner when creditors have access to complete and accurate credit information.

Topic 3, Case Study 1

Case 1:

1. She was probably denied credit because of insufficient credit experience.
2. After she moved, Ms. Carson may have taken action to see if information about her past credit use was included in her file at Anytown Credit Bureau. She may have been required to pay a small fee to "check" on her credit file, but then she'd be sure everything was in order before applying for credit in her new place of residence.

Case 2:

1. Yes. It is required only to reinvestigate the disputed information. If, upon reinvestigation, the information is found to be correct, the credit bureau does not have to delete or change the information in its file.
2. Filing a "statement of dispute" does not ensure that Mr. Brown will be granted credit. But, now each creditor who receives the report will know he disputes the information and why. It is the individual creditor who must decide whether or not to grant credit despite the unpaid bill.

Topic 3, Role Play, Direction 3

Mr. Jacobson first will have to dispute the information. The credit bureau must reinvestigate—call All Goods to find out if Mr. Jacobson did, indeed, pay cash for his television set. The student who plays the role of the credit manager at All Goods must check to see if the store made an error. (All Goods may have recorded the television repossession under the wrong name or recorded a "repossession" instead of some other activity occurring on Jacobson's account.) All Goods and the credit bureau must then correct their records. The credit bureau must tell Mr. Jacobson of his right to have corrected reports sent to recipients of the erroneous report. If Mr. Jacobson wishes, the credit bureau must send a corrected report to Hand-Crafted Furniture and any other creditors who received a report within the past six months.

Topic 4, Reading 4

1. Charlie had trouble finding and keeping a job; financial problems due to unemployment and underemployment, and lack of promotional opportunities; frustration at not knowing the cause of his problems and not being able to do anything about it. His reputation was damaged, and the information also may have affected his ability to obtain credit or insurance.
2. A credit report contains data from routine creditors' reports on a consumer's past use of credit and public record information. The investigative report contained information obtained through personal interviews, and it included subjective information regarding Charlie's reputation, life-style, personal habits, etc. This type of information may be more difficult or impossible to verify.
3. In Charlie's case, information was probably obtained from unreliable, biased, or vengeful sources. But errors could also be made when the report was written even if the information collected was accurate. Information collected also may not have been properly verified; e.g., his discharge from the Army.
4. If a person is told an investigation of personal habits, life-style, etc., will be made, he/she will be alerted to the possibility of inaccurate reporting. Also, such notification allows the applicant to protect his/her privacy by refusing to allow the investigation to be made or by withdrawing an application for credit, employment, or insurance. (The law now requires such notification. See "Flow Chart 2.")

Topic 4, Transparency 3

Question 2.

Certain information might be relevant for one inquirer (and not for another). For example, a hang-gliding hobby would be important to a life insurer, but probably not important to a creditor making a secured loan. Congress apparently felt that requiring agencies to prove their information was relevant would be unproductive. Since investigative agencies work for insurers, creditors, etc., their users would only want information relevant to the inquiry, and the marketplace would discourage agencies from collecting irrelevant information.

Pretest

Directions: Circle "T" if the statement is true; circle "F" if the statement is false.

T F 1. Credit bureaus are government agencies which keep records on how consumers use credit.

T F 2. A credit report contains information about how different creditors think a consumer will handle credit.

T F 3. Credit bureaus actually assign a "credit rating" based on a consumer's ability and willingness to repay.

T F 4. Some consumer reports include information on the habits and life-styles of consumers.

T F 5. A credit report can be obtained by anyone who wishes to know how a consumer handles financial responsibilities.

T F 6. A consumer may avoid having an investigation made of his/her habits and life-style by withdrawing an application for employment, insurance, or credit.

T F 7. When consumers fail to repay credit as agreed, that information remains part of their credit records forever.

T F 8. Because credit information is confidential, consumers can never be told the contents of their credit files.

T F 9. A consumer who disputes information contained in a credit report must first prove that the information is false in order to have it corrected.

T F 10. Credit reporting is a service which helps consumers as well as creditors.

What Is a Credit Bureau?*

What is a credit bureau?

Credit bureaus are "clearinghouses" for information about consumers and how they handle their financial responsibilities. They are private firms which collect from creditors information on their experiences with individual borrowers (Are bills paid on time?) as well as other personal and financial information (employer, income, savings, debts owed). Credit bureaus establish and maintain "credit files" on consumers who apply for or use individual or joint credit. For a fee, credit bureaus will provide "credit reports" to individuals or businesses that need such information to, for example, make decisions to grant or deny credit, employment, or insurance.

Why do creditors pay credit bureaus for this information?

In order to make good credit decisions, creditors need to know as much as possible about a prospective borrower's ability and willingness to repay. It saves creditors both time and money to use the services of a credit bureau rather than collect information themselves. Consumers also are able to obtain credit more quickly and easily when creditors have access to the information collected by credit bureaus. Today there are over 2,000 credit bureaus located throughout the United States. The majority are small, local companies servicing towns with populations of 20,000 or less. There are, however, several large regional bureaus, and some credit bureaus operate nationwide. The five largest credit bureaus account for over 150 million individual credit records, and operations are computerized to update information constantly and to prepare reports within seconds.

Does a credit bureau have a file on you?

If you ever have applied for credit, you probably have a "credit file" somewhere. A credit bureau can use your application to set up a credit file with your name, address, phone, employer, income, etc. You establish a "credit record" or "credit history," however, only by using credit. A "good" credit record is established only by repaying debts as agreed. To find out if a credit file exists on you, look in the phone book under "Credit Reporting Agencies" for the names of credit bureaus in your area. If you have applied for credit or used credit in the past, one or more of the credit bureaus listed should have information on you. Call the credit bureaus listed and ask if they have information on you. Be sure to give them any names you use or have used in the past (birth-given name, combined surname, etc.). If a credit bureau has no information on you, it can start a file by obtaining personal and employment data from you over the phone or in writing.

What types of information do credit files contain?

Most of the information contained in credit files is favorable and helps consumers obtain credit. Information about loans and credit bills that have been paid as agreed and information on earnings, other income, and assets help creditors determine quickly the creditworthiness of applicants. However, credit bureaus also collect information on unpaid bills, defaults, repossessions, unpaid taxes or judgments, bankruptcies, and criminal records. Such information may indicate that a consumer is a bad credit risk, and a creditor can use it as a basis for denying credit.

What are some of the sources of credit information?

A major source of information are creditors, who regularly provide information to credit bureaus on their active credit accounts. In addition, information is obtained from other credit bureaus, employers, landlords, references listed by consumers on credit applications, public records, and debt collection agencies. Legal records, particularly ones pertaining to suits and judgments, bankruptcies, arrests and convictions, divorces, and property transactions, are the most significant public record sources for a credit bureau's files.

Do credit bureaus assign you a "credit rating"?

The function of a credit bureau is to collect and maintain information on how consumers use credit. They do not evaluate the creditworthiness of individual consumers. Credit bureaus do, however, "rate" individual accounts depending on how they've been paid or the "manner of payment." A rating of "1" means an account has been paid within 30 days of billing or as agreed. Creditors and others who use credit reports may or may not assign credit ratings based on information obtained from credit reports, as well as from credit applications and interviews.

*Privacy Protection Study Commission, *Personal Privacy in an Information Society: The Report of the Privacy Protection Study Commission*, July 1977, pp. 55-72.

Sample Credit Report

REPORTING BUREAU

CREDIT BUREAU SERVICES OF MINNESOTA
300 MIDWEST BUILDING
ST PAUL, MN 55101
00

CONFIDENTIAL CREDIMATIC REPORT TYPE

SPECIAL REPORT INDIVIDUAL INQUIRY

BUREAU NUMBER	DATE RECEIVED	DATE ISSUED
90--90865	10/31/80	10/31/80

INQUIRER

18-89-2

CONSUMER RELATION DEPT
300 MIDWEST BLDG
ST PAUL, MN 55101

000

DATE TRADE CLEARED	DATE EMP VER (MO YR)	INCOME VERIFIED
SEE BELOW	10/80	X YES ☐ NO

THIS INFORMATION, THE COMPLETE ACCURACY OF WHICH IS NOT GUARANTEED, HAS BEEN OBTAINED FROM RELIABLE SOURCES AND IS FURNISHED PURSUANT TO THE TERMS OF APPLICABLE LAW. THE RECIPIENT AGREES TO INDEMNIFY REPORTING BUREAU FOR ANY DAMAGE ARISING FROM MISUSE OF THIS INFORMATION.

FILE SINCE (MO YR)	COMPUTER I.D. NO	SOCIAL SECURITY NO
11/79	18-23027089	999-99-9999

SUBJECT

CONSUMER, CHARLES EDGAR, SR.

SPOUSE'S NAME

MARY

CURRENT ADDRESS

65 MAIN, ST PAUL, MN 55101

808/80

COMPLETE TO HERE FOR TRADE REPORT AND SKIP TO CREDIT HISTORY

PRESENT EMPLOYER	POSITION HELD	SINCE (MO-YR)	MONTHLY INCOME
TEXAS INSTRUMENTS	SYSTEMS ANALYST	01/77	$ 2,500

COMPLETE TO HERE FOR EMPLOYMENT AND TRADE REPORT AND SKIP TO CREDIT HISTORY

DATE OF BIRTH (MO-YR)	NUMBER OF DEPENDENTS INCLUDING SELF →		
01/33	4	X OWNS OR BUYING HOME	☐ RENTS HOME

FORMER ADDRESS	FROM (MO-YR)	TO (MO-YR)
657 ELM, ST PAUL,MN	06/79	08/80

FORMER EMPLOYER	POSITION HELD	FROM (MO YR)	TO (MO YR)	MONTHLY INCOME
CITY DEVELOPMENT -VER 10/80	RESEARCH ANAL	04/75	12/76	$ 1,500

SPOUSE'S EMPLOYER	POSITION HELD	SINCE (MO-YR)	MONTHLY INCOME
---			$

CREDIT HISTORY

DESIG	KIND OF BUSINESS AND ID CODE	DATE REPORTED AND METHOD	DATE OPENED	DATE LAST CUSTOMER TRANSACTION	HIGHEST CREDIT	PRESENT STATUS: BALANCE OWING	PRESENT STATUS: PAST DUE AMOUNT	PRESENT STATUS: PAST DUE NO PMT	HISTORICAL STATUS: MOS REV	HISTORICAL STATUS: TIMES PAST DUE 30/60/90+	TYPE TERMS CURRENT STATUS (MOP)	ALT#
1	PENNEY J C D--18------41#123456789	04/80M	08/77	09/78	489	345	345	-	--	-- -- --	R$78-9	*
	COMMENT-CHARGED TO P&L											
1	NORTHWE NATL BB-18----47019987654321	04/80M	-	-	1800	1300	00	0	05	00/00/00	1$100-1	
1	SEARS ROEBUCK D--18------32#123456789	04/80M	-	09/78	700	650	--	-	12	03/02/00	R$18-3	*
1	AMER NATL BK BB-18----47004567	04/80M	01/79		LOW-4	CHECKING						

PUBLIC RECORD--12/76, JUDGMENT, $1222, *
PAID, OTHER PARTY-CONSUMER FINANCE
ST PAUL, MN

PUBLIC RECORD--04/74, BANKRUPTCY, *
IN OPERATION,
COURT- 3232,ST PAUL, MN

MISCELLANEOUS INFORMATION--11/79,
TEST FILE DO NOT REPORT

REPT FROM MEMPHIS, TN 90--00021486 ON 06/25/79, FILE 08/72, REV 11/19/79

CONTINUED NEXT PAGE

COMPUTER FORM 2000 C PLEASE SEE REVERSE SIDE FOR EXPLANATORY CODES

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Understanding Your Credit Report

The following is an explanation of the items contained in the various sections of a consumer credit report:

Identification Section:

The "File Since" date shows the date your record first became a part of this bureau's files.

If a date is in the block following the current address, this would indicate the earliest known date you had lived there. The rest of the Identification Section is self-explanatory.

CREDIT HISTORY												
DESIG	KIND OF BUSINESS AND ID CODE	DATE REPORTED AND METHOD	DATE OPENED	DATE LAST CUSTOMER TRANSACTION	HIGHEST CREDIT	PRESENT STATUS			HISTORICAL STATUS		TYPE TERMS CURRENT STATUS (MOP)	ATTR
						BALANCE OWING	PAST DUE		MOS REV	TIMES PAST DUE		
							AMOUNT	NO PMT		30/60/90+		
A	B	C	D	E	F	G	H		I	J	K	

Credit History Section:

This section contains the bulk of all credit information contained in a credit record. The following outlines the types of information you may find in your report (not all items listed are in every report):

1. **Trade Information**—each item reported will be listed in separate columns, as illustrated above. The following explanation will assist you in understanding your credit trade history.
   A. Account designation is explained on the reverse side of your report under "Account Designation Codes."
   B. Firm name lists the business reporting your account information to us.
   C. Date the report was given to Credit Bureau Services by the merchant.
   D. The date your account opened with the merchant.
   E. The date of last activity on that account, if present (i.e., last charge date, etc.).
   F. Highest balance you have had with the merchant.
   G. Current balance owing as of date merchant reported to us.
   H. Dollar amount and number of payments past due, if any.
   I. Number of months the credit history was being reviewed.
   J. If your account has ever been 30, 60, or 90 days past due, the number of times will appear under the appropriate column.
   K. MOP (Manner of Payment) This will be identified first by the type of account (I-installment, R-revolving, O-open account). Secondly by your current monthly payment amount, if any, and finally by an identifying number 0 thru 9 indicating your current credit status, as of the date reported. See reverse side of your report under "Common Language for Consumer Credit" for further explanation of each code.

2. **Bank Accounts**—either checking or savings account(s), showing the bank's name, date reported to us, the date opened, and the average balance of the account. Examples of average balance:
   LOW 2-$10 to $30 MED 2-$30 to $70 HI 2-$70 to $99
   LOW 3-$100 to $300 MED 3-$300 to $700 HI 3-$700 to $999
   LOW 4-$1000 to $3000 etc.

3. **Public Record Items**—only items of public record that are interpreted as having an effect on an individual's ability or responsibility to pay their debts, such as bankruptcy, judgments, tax liens, divorces, etc. Most of the information contained in a public record item is self-explanatory, such as the date of disposition, other party involved, dollar amount (if any), etc.

4. **Out-of-Town Report**—credit history information reported to us by another credit bureau, usually from an area where you previously resided. It tells where the report came from, when it was reported to us, how long that bureau had a file on you, and when the report was last revised (updated). Any trade lines contained in the out-of-town report will show a "kind of business" classification rather than the merchant's name; these classifications are explained on the reverse side of your credit report.

5. **Inquiries Made on Subject**—this lists any firms who have inquired with us and received information from your report. For example, if you applied for a charge account at Joe's Jewelry, they would call us for a report on you. This would constitute an "inquiry."

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Manner of Payment

Numerical Rating	
0	Too new to rate; approved but not used; unrated
1	Pays (or paid) within 30 days of billing; pays account as agreed
2	Pays (or paid) in more than 30 days, but not more than 60 days, or not more than one payment past due
3	Pays (or paid) in more than 60 days, but not more than 90 days, or two payments past due
4	Pays (or paid) in more than 90 days, but not more than 120 days, or three or more payments past due
5	Account is at least 120 days overdue but is not yet rated "9"
7	Making regular payments under Wage Earner Plan or similar agreement
8	Repossession (Indicate if it is a voluntary return of merchandise by the consumer.)
9	Bad debt; placed for collection; skip

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Would You Grant Credit?

Directions: Assume you are a loan officer at American National Bank. Mr. Charles E. Consumer, who currently has a checking account at your bank, has applied for a $5,000 automobile loan to be repaid in 36 months at an interest rate of 16% per year. On the basis of the "three Cs of credit" (character, collateral, capacity to pay) and using the credit report on Mr. Consumer, decide whether to grant or deny this loan. Please list specific information appearing on the credit report which helped you make your decision. Be prepared to explain why you took the action you did on his application.

Action taken on loan application: Approved / Rejected

Information from the credit report which helped you make your credit decision:

1.

2.

3.

4.

5.

Consumers Testify on Credit Report Errors*

Consumer Testimony 1

Several times I have tried to buy various items on credit. The salespeople were very courteous to me until the credit report was in their hands. They told me very bluntly that they would sell nothing to me on credit under any circumstances. They gave me no explanations for their decision.

After several such experiences I finally threatened legal action. One store told me that a credit report showed I had filed bankruptcy and since that filing had several legal judgments against me. They did not believe my explanation that the information was false.

I went to the credit bureau to try to see this erroneous report that was being circulated with my name on it. I was told I could not see the report because it was confidential.

I spoke to several attorneys, and they said there was no legal action I could take. I spoke to a judge who said that if I could obtain a copy of the report, an attorney could begin legal action against the credit bureau in my name. Unfortunately, everyone I talked to who could have ordered a report on me was immediately suspicious and did not want to get involved.

As far as I know, that false report is still on file at the credit bureau, and it is available to anyone in the entire country except me.

Consumer Testimony 2

The problem of inaccurate or misleading credit information can cause great harm to consumers. Some years ago, the husband of one of my own staff members had a responsible position in this very body (the Senate). He had refused to pay an auto repair bill for what he thought was a faulty transmission overhaul. His was a sad story from the beginning. The repair work made the car uncontrollable. It went into high gear and stayed there even in the crawling traffic of a downtown city. The firm refused to correct its work, but promptly processed the charge slip for the repair with Central Charge. The charge slip, incidentally, gave no clues as to just what work had been done because the charges were not itemized. Mr. X asked Central Charge the same day not to pay the auto dealer. Had he issued a check on a bank, he could have stopped payment. Central Charge claimed the funds had already been transferred. Mr. X, who understandably doubted the bill was paid so quickly, decided not to pay. After many months, Central Charge sued him in court. When he turned up for trial, almost eager to tell his story in public, Central Charge dropped the suit. The case was dismissed. He naturally thought that was the end of his troubles.

However, several years later he was under consideration for a high executive position in government and the unpaid bill turned up during an investigation of his background. He was required to prepare a lengthy memorandum explaining the so-called delinquency and to obtain a copy of the court order dismissing the case. Fortunately for him, his explanation was accepted, or he might not have been hired.

Consumers Testify
(Continued on next page)

*These three accounts are from the U.S. Congress, Senate, Subcommittee on Financial Institutions of the Committee on Banking and Currency, *Fair Credit Reporting-1969: Hearings on S. 823*, 91st Cong., 1st sess., 20 May 1969, pp. 127-28, and 23 May 1969, pp. 381, 384-85, 388. The situations described are extreme and are used for the purpose of illustration only.

Consumers Testify (continued)

Consumer Testimony 3

MRS. COLLINS: We had applied for a car loan and it was refused. The bank did not furnish us with any other information. I have a relative who works for a store that uses credit reporting services. She was able to find out that a trucking firm had a judgment for a gentleman named William Collins living on Cherry Street in the city. This was put on the credit file of all the William Collinses. Although our name was Billings J. Collins, we were also swept into this mass recording.

SENATOR PROXMIRE: Your name was?

MRS. COLLINS: Billings J. Collins. But you see we also use the name "Bill."

SENATOR PROXMIRE: I see.

MRS. COLLINS: This came up again when we applied for a mortgage loan.

SENATOR PROXMIRE: What action did you take with regard to the credit bureau to check this?

MRS. COLLINS: We didn't because there is no redress.

SENATOR PROXMIRE: What did you try to do?

MRS. COLLINS: We tried to find out the name of the credit bureau, but no one could reveal it.

SENATOR PROXMIRE: Has the information ever been corrected?

MRS. COLLINS: Not that I am aware of.

SENATOR PROXMIRE: As far as you know it is still on your record?

MRS. COLLINS: I have no way of knowing. We have found other ways to survive and our income is sufficient. We are not threatened; we have the Teachers Credit Union that honors us. But it has made me aware of what can happen to others who cannot survive.

Your Fair Credit Reporting Rights

Whenever you are denied consumer credit at least in part because of information in a credit report, you must be given:

- the name, address, and phone number of the credit bureau which provided the information, and
- the reason for denial, or information on your right to request the reason for denial.*

* Required under the Equal Credit Opportunity Act. See Section 2, The Equal Credit Opportunity Act, Topic 5.

If you contact the credit bureau, it must:

- let you know the nature and substance of all information contained in a credit report (except medical information).
- inform you of the sources of information (except for investigative consumer reports).*
- provide you with the names of employers, creditors, and others who have recently received reports.
- reinvestigate any information you dispute within a reasonable time.

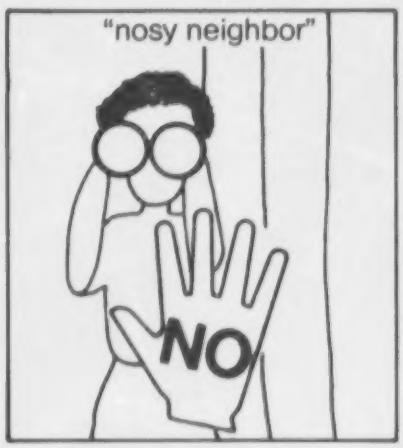
If the credit bureau finds the information is:

- inaccurate or cannot be verified, the information must be corrected or deleted.
- accurate, the credit bureau must allow you to write a brief statement of dispute and include it in all future reports.

*See Topic 4, this section.

if any deletion or notation is made regarding the information, you may request that the new information be sent to:

- any employer receiving information during the past two years.
- any other person receiving a report during the past six months.

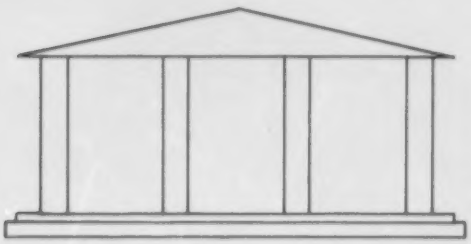


Credit bureaus can provide information only to:

- creditors who are considering granting or have granted you credit.
- employers considering you for employment.
- insurers considering issuing you an insurance policy.
- government agencies reviewing your financial status in connection with issuing you a license.
- anyone else with a legitimate business reason for needing the information.

The credit bureau must automatically delete:*

- information on a bankruptcy which is more than 10 years old.
- other adverse information which is more than seven years old.



If you believe a credit bureau or a credit report user has not complied with the law, you may:

- notify the Federal Trade Commission (credit bureaus and many users are under their jurisdiction).
- sue for actual damages (including attorney's fees and costs).

If a person or firm knowingly requests information under false pretenses, or if a credit bureau knowingly gives information to someone not authorized to receive it:

- you may ask a U.S. county or district attorney to sue the unauthorized user or the credit bureau.
- the unauthorized user or the credit bureau may be fined up to $5,000 or imprisoned for up to one year.

*These rules do not apply to information provided for loans over $50,000, underwriting over $50,000 of insurance, or employment decisions when the salary exceeds $20,000.

Who Has the Stronger Interest?

Consumer's Right to "Start Over"

Creditor's Right to Know about Past Use of Credit

Under the Fair Credit Reporting Act . . .

Most "adverse information" must be deleted after **7** years

- Unpaid bills
- Unpaid taxes
- Unpaid judgments
- Public record information

If you declare bankruptcy, that information remains on file for **10** years!

What If Your Credit Report Is Wrong?

You receive written notice that credit has been denied on the basis of information obtained from a credit bureau.

↓

The creditor must tell you the name, address, and phone number of the credit bureau.

↓

You may arrange to visit the credit bureau to learn the contents of your credit report.

↓

A trained interviewer will explain to you the contents of your credit report. Or the credit bureau may send you a copy of the report along with an explanation of items contained in it.

↓

Information is correct.

If the credit bureau claims the information is correct, you may submit a "statement of dispute."

↓

The credit bureau must include the statement or a summary of it in all future credit reports.

You believe information is incorrect.

↓

The credit bureau must reinvestigate disputed information.

↓

The credit bureau must correct, delete, or update any information which is incorrect or cannot be verified.

↓

You may request that the credit bureau send corrected reports to creditors who have received reports during the past six months.

You believe information is incomplete.

↓

Supply names of creditors who have not provided information to the credit bureau.*

↓

The credit bureau must contact those creditors for information on your credit accounts.

*See Section 2, The Equal Credit Opportunity Act, Topic 4

Case Study

Case 1

Betty Carson applied for credit at Friendly Finance Company. She was turned down for credit and received a form letter stating that information had been obtained from a consumer reporting agency. The letter included the name, address, and phone number of Anytown Credit Bureau.

Betty called Anytown Credit Bureau to find out what information it had given the finance company. She was told that it generally did not give out such information over the phone, but she could come to the office to learn the contents of her credit file. Betty said she would be able to come at 1:00 p.m. on Monday.

When Betty arrived at the credit bureau, she was asked to show a driver's license and one other piece of identification. A trained interviewer talked with her and revealed that the inquiry from Friendly Finance Company was the only inquiry received during the past six months. The only other information in her file was that an account held five years ago with AAA Department Store had been paid. Betty was surprised at the lack of credit information in her file. But she explained that until recently she had lived in a different state. The interviewer asked if she could provide the names of her creditors there. The credit bureau would then check with those firms and add any new credit information. Betty did so and applied for credit again at Friendly Finance Company. This time, she was granted credit.

1. Why do you think Ms. Carson was denied credit?

2. How could she have avoided being denied credit the first time?

Case 2

Harry Brown was turned down for credit because of a report at Truth, Inc., a local credit bureau. When he called Truth, Inc., he found that the one piece of adverse information in the report was that he had not paid a roofing contractor for work done on his home over a year ago. Harry explained that he had refused to pay because the roofing contractor had not fulfilled his part of the contract. The interviewer said that Truth, Inc., would be happy to reinvestigate and question the roofing contractor about the information in Harry's file.

A week later Harry received a form letter from the credit bureau stating that it had reinvestigated the disputed matter and had determined that the information contained in his file was correct. The bureau explained, however, that Harry could submit a statement of not more than 100 words explaining his side of the dispute. That statement, or a summary of it, would then go along with each new report. With the help of the credit bureau Harry drafted the following statement:

> "ABC Contractors agreed to reroof my house for $5,800. When I got their bill, it was $7,200. I refused to pay the additional $1,400 because they can't tell me for what work I am paying the additional money. Also, their workmanship was poor. The new roof leaked, and the flashings were put on incorrectly. I have had to pay another contractor to correct the problems even though ABC Contractors supposedly gave me a three-year warranty."

One week later, Truth, Inc., notified Harry that his statement had been received, and that it would be incorporated into all future credit reports. He also was told of his right to have updated reports sent to potential creditors who received reports during the past six months and potential employers who received reports during the past two years. Harry indicated he wanted one creditor to receive an updated report.

1. Did the credit bureau act legally in not deleting the unpaid bill from Mr. Brown's credit file?

2. Do you think Mr. Brown will obtain credit now that his "statement of dispute" is included in his credit report?

Charlie Green and the Mysterious Report*

Charlie Green, a salesman in his late thirties, began work for a large manufacturing firm in 1962. He had lost a previous sales position because of a company merger. The new firm felt fortunate to have an employee with such excellent experience and skills.

However, one week after he started with the firm, the sales manager accused Charlie of giving false information on his application. Charlie denied that he had done so intentionally, but stated he might have made an error. He asked what information was being questioned, but the sales manager refused to tell him. From that day on the sales manager became more and more hostile toward Charlie. Finally Charlie resigned.

Charlie began interviewing for positions with other large national companies. After several rejections, he took a job with a smaller company at a lower salary. He continued to apply to larger firms for several years with no success.

In 1967, after being told he was an "excellent candidate," one firm reported they could not hire him because of information contained in an investigative report. It refused to tell him anything more about the report.

Charlie then persuaded a friend who had his own business to order a similar report as though he had applied for a job. This was the first time he learned the basis for his employment difficulties. The report stated that (1) he had been dishonorably discharged from the Army, (2) he was responsible for a noisy, late-night party while a tenant in an apartment complex, and (3) his former landlord was glad he had moved out in view of his unruly conduct. Army records could prove Charlie had an honorable discharge. Charlie recalled that an elderly neighbor complained to the police when he had hosted a small gathering for friends several years ago. She was known to complain about any noise, even if you walked in your apartment with your shoes on! Charlie had never had any problems with his former landlord and doubted if he was the source of the derogatory remarks.

1. What problems did the investigative report cause for Charlie?

2. How does this investigative report differ from a credit report?

3. What are some explanations for the errors made in Charlie's report?

4. Do you think a consumer who is applying for a job should be told if an investigation including personal interviews will be conducted?

*This account is from the U.S. Congress, Senate, Subcommittee on Financial Institutions of the Committee on Banking and Currency, *Fair Credit Reporting—1969: Hearings on S. 823*, 91st Cong., 1st sess., pp. 84-87. This situation is extreme and is used for the purpose of illustration only.

Investigative Reporting

Credit bureaus collect and provide data primarily about a person's bill-paying habits. When a consumer applies for insurance, employment, or credit to purchase a major item, however, additional information may be required. For example, to determine whether an applicant is a good risk, an insurance company may want to know his/her drinking habits, driving record, and hobbies (such as hang-gliding or motorcycle racing). Since this information is generally not contained in a credit report, employers, insurers, or creditors hire a firm which investigates the applicant and prepares an investigative report. Firms which prepare these reports are called investigative reporting agencies.

Besides reviewing the credit bureau's file and checking the sources used by credit bureaus (creditors' records, public records, etc.), investigative agencies conduct interviews with the applicant's friends, neighbors, and co-workers. In the past, people often were asked to make value judgments about the actions, habits, or life-style of the subject of an investigative report. If an interviewer asked one person about an applicant's drinking habits, he/she might respond that the applicant drinks "moderately." However, another acquaintance may describe the same person's drinking habits as "excessive." To avoid situations like this, investigative agencies now try to ask questions to obtain specific information rather than judgments on an applicant's habits or life-style. For example, instead of asking someone to describe an applicant's drinking habits, an investigator will ask, "How many drinks does John Doe have during the course of an evening?"

Unlike credit bureaus, investigative agencies are not required by law to reveal the names of their sources. It was believed that if people thought their identities would be revealed, they might be reluctant to make any statements that might hurt the subject of the investigation. Thus, information would possibly be less valuable to creditors, employers, or insurers. However, there is also the possibility that a neighbor or co-worker whose identity will not be revealed might use an interview with an investigator as an opportunity to give false and potentially damaging information.

To protect consumers against inaccurate information and to protect their right to privacy, the Fair Credit Reporting Act includes some special provisions with regard to investigative reporting. First, whenever a creditor, insurer, or employer orders an investigative report, he/she must also notify the consumer within three days that a report has been ordered. The consumer must be told the report will include information on his/her character, personal habits, and life-style. Second, the consumer may request additional information about the investigation. Third, if denied credit, employment, or insurance on the basis of investigative information, the consumer must be told the name and address of the agency which prepared the report. He/she then has the right to learn the contents of the report and have disputed information reinvestigated. Information that cannot be verified by the investigative agency must be deleted. As with credit reports, if an investigative agency claims the information is true, the consumer may write a statement explaining why he/she believes it is false. This statement must then be included in all future reports.

Generally, an investigative reporting agency is a separate company with no connection to a credit bureau. However, anytime a credit bureau uses personal interviews to obtain information about a consumer's life-style, etc., it becomes an "investigative agency" and is subject to the special provisions described above of the Fair Credit Reporting Act.

'Hi there! I'm just making a credit check and . . .'

[From Parade Magazine, Nov. 3, 1968]

1. What is the cartoonist saying about credit reporting?
2. Should investigative agencies be prohibited from collecting certain types of information?

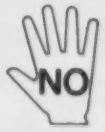
Reprinted with permission of Parade Magazine.

What If an Investigative Report Is Ordered?

You apply for credit, insurance, or employment.
The creditor, insurer, or employer orders an investigative report on you.
Within three days you are notified in writing that the report was ordered and of your right to request additional information about the investigation.
You request and receive additional information about the nature and scope of the investigation.
You refuse to let the investigation be made.
Credit, insurance, or employment can be denied on the basis of your refusal.
You decide to let the investigation proceed. Investigation is conducted, and the creditor, insurer, or employer receives a report on you.
You withdraw your application.
The investigative report is canceled.
You are notified in writing that credit has been denied on the basis of information received from an outside source other than a credit bureau. You are told you can request the nature of the information within 60 days.
Credit, insurance, or employment is granted.
You learn the nature of the information, but not the names of persons providing the information.
Information is correct.
You believe information is incorrect.
The investigative agency must reinvestigate disputed information.
If the investigative agency claims that the information is correct, you may submit a "statement of dispute."
The investigative agency must delete or correct any information that cannot be verified.

CONFIDENTIAL

Does the person or organization requesting a credit report on a consumer have a legitimate business reason for needing the information?



Creditor making a credit decision

Employer making a hiring decision

Insurer making an insurance decision

Debt collector

Nosy neighbor

Owner or employer of any firm

BUT . . .

ACCESSIBLE

Can a consumer learn what information is in his/her credit report in order to be sure it is correct and up-to-date?

A reporting agency must reveal at no charge the contents of a consumer's report if on the basis of that report he/she has been denied credit, employment, or insurance.

A consumer may at any time check on the accuracy of information in his/her report, but the reporting agency may charge a fee for this service.

Shifting Regulatory Costs

Reveal Contents of Credit Reports
Correct Reporting Errors
Send Updated Credit Reports
Reinvestigate Disputed Information

"Costs of Doing Business" Increase after the Fair Credit Reporting Act

CREDIT BUREAU

SHIFT COSTS TO

Takes Longer to Obtain Credit Information

Credit Reports Cost More

Less Information Provided in Reports

More Unpaid Bills

"Possible Costs of Doing Business"

CREDITOR

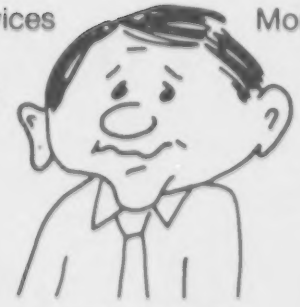
SHIFT COSTS TO

Pay More for Goods/Services

Pay More for Credit

More Difficult to Obtain Credit

Less Credit Available



CONSUMER

YOUR CREDIT RIGHTS

SECTION 4

The Fair Debt Collection Practices Act

Introduction

In 1977, the Fair Debt Collection Practices Act was enacted to prevent abuses in the debt collection industry. In this section, students first learn why consumers sometimes do not pay their credit bills despite their intentions to repay. In a role-playing activity, students learn what consumers should do if they experience temporary bill-paying problems, and how creditors are usually willing to help if they are made aware of consumers' problems. Students also will learn how consumers can either dispute debts they believe are invalid or stop communications about a debt.

Key Concepts

1. Loss of income and overextension are the major causes of consumer delinquency. Planning and controlling the use of credit, having funds available to pay bills if income or expenses change, and having adequate insurance can provide protection against delinquency.
2. A consumer should notify the creditor immediately of any bill-paying problem and of his/her intent to repay. A creditor often will renegotiate payment terms to allow a consumer who has a temporary bill-paying problem to postpone payments or make smaller payments.
3. After the first communication about a debt, a debt collector who is working for a creditor must provide the consumer with the name of the creditor and the amount of the debt. If the consumer disputes the debt, the debt collector must verify it before taking further action to collect the debt.
4. The Fair Debt Collection Practices Act does not prohibit debt collection activity, but does prohibit a debt collector from publicizing a consumer's indebtedness, harassing a consumer by calling at an inconvenient time or place, or using other abusive or unfair practices to collect a debt.

Topic 1—If You Can't Pay . . .

Objective: Student will know what the major causes of consumer delinquency are and identify ways consumers can prevent or reduce the risk of default. Student will know what a consumer should do if he/she cannot pay credit bills.

Materials Needed:

Transparency 1—"Why Consumers Don't Pay"
Transparency 2—"If You Can't Pay . . ."
Budget Worksheet

Directions:

1. Most consumers who use credit do repay, or intend to repay creditors. Tell students how relatively few unpaid credit bills or loans are the result of fraudulent credit use by people who do not intend to repay. Ask students to list *other* reasons why a consumer might not repay credit as agreed. [Possible responses include: resignation, separation, or lay-off from a job; reduction of real wages or hours worked; illness or disability; using too much credit; unexpected expenses; dissatisfaction with the goods or services purchased; goods or services are never received; incorrect credit bill.] Show students Transparency 1, which lists the major reasons for consumer default and the percentages of defaults attributed, at least in part, to each factor. Percentages are based on consumer responses to questionnaires regarding the actual reasons for default.*
2. Using the questions below, discuss how a consumer can reduce the likelihood of not being able to repay:
   a. Income may be lost or reduced because of events and circumstances beyond a consumer's control. What can a credit user do to minimize or eliminate the problems caused by a temporary loss of income? [Whenever future income is relied upon to repay credit, a certain amount of money could be set aside and available just in case income is reduced. Also, adequate insurance may offer protection against income loss and/or pay bills in the event of illness, disability, or death.]
   b. How can a consumer protect himself/herself against using too much credit, or overextension? [A consumer may not want to use income that is not reliable (e.g., part-time or overtime earnings, bonuses, a second wage-earner's earn-

* Data from U.S. Congress, Senate, Subcommittee on Consumer Affairs of the Committee on Banking, Housing, and Urban Affairs, *Fair Debt Collection Practices Act: Hearings on S. 656, S. 918, S. 1130, and H.R. 5294*, 95th Congress, 1st Sess., 12-13 May 1977, pp. 230-45.

ings, etc.) as a basis for obtaining more credit. Also, once monthly credit bills reach the maximum amount a consumer can safely spend to repay credit each month, the consumer should postpone additional credit purchases until other credit bills are paid.]

3. Consumer credit counselors recommend that consumers notify their creditors as soon as bill-paying problems develop. How missed or late payments are handled eventually depends on the individual creditor. However, being notified of the problem as soon as it occurs may influence a creditor's decision to report a "late" payment to a credit bureau or start debt collection efforts. Show Transparency 2 to students. Discuss other steps credit counselors may suggest consumers take to help protect their credit records and to resume making payments as soon as possible. You may want to ask students if they can add to the list other "tips" for reducing the negative consequences of temporary bill-paying problems.
4. Give each student a Budget Worksheet used by the Minnesota Financial Counseling Service to help consumers analyze their spending habits and prepare a realistic budget. Ask students to identify categories or items for which spending could be reduced if a consumer has a bill-paying problem. [See "Answer Key."] Adults or students who are responsible for all or part of their support may want to complete this worksheet in order to analyze their own spending patterns.

Topic 2—Can the Creditor Help?

Objective: In a role-playing activity, students will assume the roles of consumers, creditors, and a debt collector to demonstrate "actions" each party can take to help resolve temporary bill-paying problems.

Materials Needed:
Role Play Cards (Sets of 7)
Role Play Observation Sheets
Role Play Follow-up Sheet

Directions:
1. Conduct three role plays which simulate debt situations. Select seven students to assume the following roles:

[Role Play 1]	Consumer 1 Creditor 1 (electronics store)
[Role Play 2]	Consumer 2 Creditor 2 (department store)
[Role Play 3]	Consumer 3 Creditor 3 (travel agency) Debt Collector 3

Give each student assigned a role the appropriate Role Play Card. All other students will be "observers." They should be given one Role Play Observation Sheet for each role play they will observe.

2. For each role play ask the "consumer" and "creditor" (and "debt collector" in Role Play 3) to read their cards and then "enact" the debt situation described. Students should reveal through actions or words the information contained on their cards, and act out the steps the consumer/creditor/debt collector would take to solve the problem (on the basis of the information given on their Role Play Cards). For example, Consumer 1 should make it known that he/she has paid bills on time in the past; Creditor 1 should then "negotiate" with Consumer 1.
3. After students have conducted and observed each of the three role plays, ask "observers" to describe what happened in each role play and what their reactions were to the role players' actions in each debt situation. Allow students who assumed the

Vocabulary

Communication	Any oral, written, or telephone contact with a consumer regarding a debt.
Consumer Delinquency	A situation in which a consumer has one or more past due credit accounts and has made no satisfactory arrangements for repayment.
Convenient Time	The hours between 8:00 a.m. and 9:00 p.m. when some contacts with a consumer regarding debt are permitted.
Debt	An obligation to pay money to another person or company.
Debt Collector	Anyone who regularly collects or attempts to collect debts owed to another person or company, or a creditor who uses a different name when collecting debts owed directly to him/her.
Debtor	A consumer who owes money to another person or company.
Default	Failure by a consumer to comply with the terms of a credit agreement.
Dun	To ask a consumer persistently and repeatedly for payment of a debt.
Harassment	Action taken against a person in an effort to disturb or irritate such as using or threatening violence, using obscene language, or telephoning continuously and repeatedly.
Location Information	A person's home address, telephone number, or place of work—and the only information a debt collector may ask for from a person other than the debtor.
Repossession	A legal action in which a creditor takes back goods purchased on credit for which payment is past due.
Wage Garnishment	A court-sanctioned procedure in which a portion of a consumer's wages is paid directly to his/her creditors.

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roles of creditors, consumers, or the debt collector to give reasons for their actions. Discuss the role-playing activity using the following questions:

a. Why were Creditors 1, 2, and 3 willing to negotiate with their customers? [They probably would accept smaller payments because the consumers' bill-paying problems appeared to be only temporary. They preferred to make the arrangement than to incur the costs of immediate legal action to obtain payment—and possibly lose the consumer's future business.]

b. How is Role Play 3 different from Role Plays 1 and 2? How does this affect the way in which the debt is collected? [The debtor is not a "customer" of the person or firm collecting the debt. The debt collector, unlike a creditor who collects his/her own debts, may not be as concerned about maintaining a good public image or a good relationship with the debtor. A creditor may tell a debt collector not to accept smaller payments, etc. However, a creditor may also instruct the debt collector not to do anything that may jeopardize the creditor-customer relationship or the creditor's public image. Then the debt collection situation would be similar to Role Plays 1 and 2.]

c. The provisions of the Fair Debt Collection Practices Act apply to all debt collection agencies, but not to creditors who collect their own debts. Why do you think this is so? [Congress believed that creditors collecting debts from their "customers" would be concerned about (1) their public image, because they solicit business from the general public, and (2) customer goodwill, because they want to keep the consumer as a customer. Congress believed that these concerns alone would encourage creditors to treat their delinquent customers fairly.]

4. Use the Role Play Follow-up Sheet to discuss the following items:

a. What consumers may want to do in the situations described in order to protect their credit records and resume making payments as soon as possible.

b. Why creditors may or may not be willing to renegotiate payment terms in certain debt situations.

c. What debt collectors can and cannot do when contacting consumers about debts.

Topic 3—The Fair Debt Collection Practices Act

Objective: Student will know when and how a debt collector can approach a consumer about a debt and will identify illegal debt collection practices.

Materials Needed:
Reading 1—"Your Fair Debt Collection Practices Rights"
Student Exercise 1
Transparency 2—"Freedom to Do Business . . . Freedom from Abuse"

Directions:
1. The Fair Debt Collection Practices Act of 1978 was intended to prevent the use of abusive and unfair debt collection practices. It also gave certain rights to the consumer who is being contacted about a debt. Distribute to students the reading, "Your Fair Debt Collection Practices Rights." As class read and discuss the rights and the responsibilities of both consumers and debt collectors.

2. Assign Student Exercise 1 to assess student understanding of the provisions of the Fair Debt Collection Practices Act. When students have completed the exercise, review their responses by asking individual students to explain why a debt collection activity is "legal," "illegal," or why its legality "cannot be determined." Emphasize that a certain activity may be illegal if it involves a "covered" debt collector, but legal if it involves a creditor collecting his/her own debts. [See "Answer Key."]

3. Show Transparency 3, which illustrates how the Act protects the rights of consumers and the rights of debt collectors to collect valid debts. Use the questions below to discuss the limits of the Fair Debt Collection Practices Act:

a. Can a consumer stop a debt collector from trying to collect a valid debt? [No. All a consumer may do is have the debt collector cease further communications about the debt. A creditor or debt collector may decide to take legal action to collect the debt. In that case, the debt collector may communicate further only to explain those legal consequences to the consumer.]

b. Do you think the Fair Debt Collection Practices Act should also apply to creditors, retailers, and other lenders who collect their own debts? Why or why not? [Students may agree with Congress that the creditor's need to maintain customer goodwill and the possibility of future business will prevent most creditors from abusing or harassing consumers. However, students may also argue that being a creditor's "customer" does not always protect the consumer from being the victim of unfair debt collection practices. For instance, a creditor may be more interested in collecting the money than in "maintaining goodwill," especially if a debtor is an infrequent customer. And a creditor may not be concerned about losing the business of a consumer who does not pay.]

(Note: The Federal Trade Commission found that one-half of the customer complaints regarding debt collection involved creditors collecting their own debts, not debt collection agencies. It has recommended that Congress amend the Fair Debt Collection Practices Act so everyone who collects debts lives by the same rules. So far Congress has not amended the Act.)

Topic 4—Exercising Your Rights

Objective: Student will know what steps a consumer can legally take when a debt collector calls about a debt.

Materials Needed:
Case Study
Flow Chart—"What If a Debt Collector Calls?"
Transparency 4—Debt Validation Notice

Directions:
1. The Fair Debt Collection Practices Act helps prevent abuses in the debt collection industry. Assign the Case Study, which describes two debt collection situations and asks students about both the consumer's and debt collector's rights and responsibilities. When students have completed the activity, review their answers, referring to the reading, "Your Fair Debt Collection Practices Rights" [See "Answer Key."]

2. Give each student the flow chart, "What If a Debt Collector

Calls?" Discuss the steps consumers and debt collectors must take in order to exercise their rights and comply with the Fair Debt Collection Practices Act. Emphasize that a consumer may request a debt collector to cease communications even if the debt being collected is valid. The debt collector or creditor may still take legal action against the consumer to obtain payment, but the phone calls, etc., must stop.

3. Whenever a debt collector communicates with a consumer about a debt, he/she must send a validation notice within five days. Show students Transparency 4 and point out the following items which must appear in the notice:

   (1) creditor's name,

   (2) amount owed,

   (3) a statement that the debt will be assumed valid and correct if not disputed within 30 days, and

   (4) information on how to dispute the debt and the debt collector's responsibility if a debt is disputed.

Topic 5—The Economics of the Fair Debt Collection Practices Act

Objective: Student can list economic incentives that (1) a creditor may have for renegotiating payment terms with a debtor, and (2) a debt collector may have for treating consumers fairly and without abuse. Student can identify whether the creditor, debt collector, or consumer will bear certain costs of the Fair Debt Collection Practices Act.

Materials Needed:

Transparency 5—"Consumer Clout"
Reading 2—"It Doesn't Pay"
Student Exercise 2

Directions:

1. As discussed earlier in this section, the Fair Debt Collection Practices Act distinguishes between creditors who collect their own debts and debt collectors who collect debts for others. Creditors include banks, savings and loans, credit unions, finance companies, retailers, and professionals who attempt to obtain payment from their customers. Debt collectors, on the other hand, collect debts for creditors—financial institutions, firms, professionals, etc. Any creditor who uses a different name when collecting debts is also considered a debt collector. Show Transparency 5, which illustrates the potential "bargaining power" of a consumer who is being approached about a debt by the creditor. Discuss the consumer's and creditor's situations using the questions listed on the transparency. [See "Answer Key."]

2. Ask students if they think the situation shown in Transparency 5 would be any different if the creditor hired a debt collector to obtain payment from the consumer. Discuss students' reasons why the situation would be different. Similar? [Differences: The debt collector may not have had any past dealings with the consumer and may not be aware of his intention to repay. He/she may not be concerned about maintaining a good customer relationship or public image. The consumer's future business is not an issue. Similarities: The creditor may instruct the debt collector not to jeopardize the customer's goodwill or future business. Thus, the debt collector's future business with that *creditor* may depend on not antagonizing the consumer—i.e., treating him fairly and without abuse. The debt collector may also initiate legal action on behalf of the creditor to reduce losses and/or to collect the debt.]

3. Assign Reading 2, which is based on testimony from a professional debt collector and which describes why the use of abusive or unfair debt collection practices usually doesn't "pay." Discuss the effectiveness of various debt collection methods using the following questions:

   a. Who do you think would be more likely to collect money—a debt collector who was polite and persistent or one who threatened, frightened, or otherwise treated consumers unfairly? [There is no "right" answer to this question. Mr. Kelly's testimony suggests that harassing or frightening consumers who do not pay their bills doesn't work. However, people react differently to different tactics. Some consumers may respond to threats, harassment, etc., and pay a debt sooner or pay a debt they would otherwise not have paid.]

   b. If politeness and persistence do not work, what can a debt collector do other than resorting to the use of unfair or abusive collection tactics? [A debt collector may use legal means to try to obtain payment or reduce the creditor's losses. The creditor may repossess goods or obtain a judgment against the consumer. The debt collector may then tell the consumer that certain legal action will be taken if he/she does not pay.]

4. As with the consumer credit protection laws discussed in Sections 2 and 3, there are "regulatory costs" of the Fair Debt Collection Practices Act. To comply with the law, all debt collectors must validate debts and inform consumers of their rights. If a consumer disputes a debt, the debt collector must provide written verification of the debt. A debt collector may also incur legal costs or penalties if he/she fails to comply with the provisions of the law. Some or all of these additional costs may be shifted to creditors in the form of higher rates charged for debt collection services, slower collection of debts, or less money being collected. Consumers, too, incur costs (time, postage, legal advice, etc.) as they exercise their rights under the Act. If, because of higher collection costs or more uncollected debts, it costs creditors more to do business, they may raise prices, increase the cost of credit (within legal limits), or supply less credit to consumers. Assign Student Exercise 2, in which students identify who would bear possible "costs" of the Fair Debt Collection Practices Act. [See "Answer Key."]

   (Note: Students have learned how the Act protects them against abusive or unfair debt collection methods when they are not a "customer" of the person collecting the debt. This topic shows students how this protection is not necessarily "free." Consumers may incur costs as they exercise their rights. Some or all of the legal costs or penalties and regulatory costs incurred by debt collectors and creditors may be shifted to consumers in the form of higher prices, more expensive credit, or less available credit.)

Answer Key

Pretest

1. *False.* Having a steady income and good credit habits will usually prevent bill-paying problems. However, anyone may lose a job, become unable to work, or incur unexpected expenses that make it difficult or impossible to meet financial obligations.
2. *False.* Most delinquencies are caused by a loss of income or the inability to work due to illness or accident. According to social scientists, few delinquencies are caused by consumers who never intend to repay.
3. *True.* Most creditors try to minimize their losses and maintain good relationships with their customers. If a creditor is notified of a consumer's temporary bill-paying problem, he/she may be willing to accept smaller payments or allow the consumer to postpone one or more payments.
4. *False.* Creditors handle the reporting of delinquent accounts differently. One creditor may automatically report missed payments to the credit bureau, while another may allow an account to go 60 or 90 days or longer before reporting it.
5. *False.* A debt collector cannot call a consumer at work about a debt if (or after) he/she knows the employer prohibits such communication.
6. *False.* The Fair Debt Collection Practices Act prohibits certain debt collection activities; however, only debt collectors (persons or firms who are in the business of collecting debts for others) are covered by the Act. Creditors collecting their own debts are not covered. Creditors who use a different name when collecting debts from their customers are also covered by the Act, however, and must follow the same rules as other debt collectors.
7. *False.* In attempting to collect a debt, a debt collector may threaten legal action only if he/she or the creditor would normally take such action.
8. *False.* A consumer may write and request that a debt collector stop calling about a debt. Communications about the debt then must cease except to notify the consumer of any action that the debt collector or the creditor will take.

Topic 1, Budget Worksheet

Spending could probably be reduced on the items and categories listed below:

Housing (electricity, heating, telephone, and water)

Food (nonessential items)

Car (gas, oil, repairs, tires, etc., if nonessential driving is reduced)

Clothing (nonessential items)

Personal (nonessential items)

Entertainment (Some spending probably could be reduced in each area listed.)

Topic 3, Student Exercise 1

1. *Illegal.* A debt collector cannot use a post card to communicate with a consumer.
2. *Legal.* As long as the creditor does not go by a different name when collecting debts, he/she is not covered by the Fair Debt Collection Practices Act.
3. *Legal.* A bank collecting its own debts is not covered by the Act.
4. *Illegal.* A debt collector cannot call at an unusual or inconvenient time (before 8:00 a.m. or after 9:00 p.m.).
5. *Illegal.* ABC Stores is covered by the Act because it goes by ABC Collections, Inc., when collecting debts. (6:00 a.m. is generally considered an unusual time.)
6. *Legal.* A department store collecting its own debts is not covered by the Act.
7. *Legal.* A credit union collecting its own debts is not covered by the Act.
8. *Illegal.* A debt collector cannot call a consumer at work if such contact is prohibited by the employer.
9. *Illegal.* Because a debt collector legally cannot "throw a consumer in jail," he/she cannot threaten to do so.
10. *Legal.* The creditor may repossess the furniture so it can be stated as a possible consequence of nonpayment.

Topic 4, Case Study

Case 1:

1. Within five days, the debt collector must send Ms. Johnson a written notice stating the amount of the debt, the name of the creditor, and that the debt will be assumed valid if not disputed within 30 days.
2. If Ms. Johnson disputes the debt, she must write the debt collector within 30 days requesting verification of the debt.
3. Ms. Johnson may notify the Federal Trade Commission which supervises the debt collector or take legal action against the debt collector.

Case 2:

1. Yes. Under the Fair Debt Collection Practices Act, John may request in writing that the debt collector cease all further communications about the debt.
2. False. A creditor or debt collector may still take legal action to obtain payment or reduce losses (wage garnishment, repossession, etc.). A debt collector may also contact the consumer to say he/she (1) will be taking no further action, (2) will be taking specific legal action, or (3) may take certain legal action if in fact the debt collector ordinarily does so in such instances.

Topic 5, Transparency 5

1. Given the borrower's present record and his intention to repay, the creditor probably will "negotiate." If the creditor is a large firm, the past due account may be reported automatically to the credit bureau each month, even if no further action is taken.
2. The consumer may or may not pay. But he might tell other people about the creditor's actions, possibly affecting the creditor's public image (and future business). He also might decide not to do business with the creditor anymore.
3. The creditor can always take legal action in an attempt to obtain payment or receive the goods purchased on credit. The television set may be repossessed or the creditor may obtain a judgment against the consumer. If necessary, wages could be garnished or a bank account could be restricted.

Topic 5, Student Exercise 2

1. Creditor
2. Consumer
3. Consumer
4. Consumer
5. Debt collector (The debt collector loses business. The creditor, too, may still be incurring high collection costs as a result of the Act.)
6. Consumer
7. Debt collector
8. Consumer (The creditor has shifted the higher costs of debt collection to consumers. However, the creditor may still incur costs if reducing the availability of credit also causes business to decrease.)

Pretest

Directions: Circle "T" if the statement is true; circle "F" if the statement is false.

T F 1. A steady income and living within one's means will prevent a consumer from having any bill-paying problems.

T F 2. Most consumers who fail to pay their credit bills never intend to repay.

T F 3. The creditor is the first person a consumer should notify when he/she cannot pay a bill or make an installment loan payment.

T F 4. Whenever a consumer pays a bill late, the creditor reports this information to the credit bureau.

T F 5. If a debt collector cannot reach a consumer at home, he/she may always call the consumer at work about a debt.

T F 6. Both creditors who collect their own debts and debt collectors must follow the same rules when inquiring about a consumer's debt.

T F 7. A debt collector can always threaten legal action in an attempt to obtain payment.

T F 8. A consumer who owes a debt, can do nothing to stop a debt collector from calling about the debt.

Why Consumers Don't Pay

Reason for Default	Primary or Contributing Cause of Default (% of Cases)	
Loss of income		48%
Unemployment	24%	
Illness	16%	
Other	8%	
Overextension		25%
Defective goods or services or other perceived consumer fraud		20%
Fraudulent use of credit		4%
Other		3%

If You Can't Pay . . .

- Notify creditor before a bill or loan payment is due.
  - State why you can't pay, your intent to pay, and when you will pay.
  - If possible, continue to make smaller but regular payments.
- Eliminate all further credit purchases.
- Cut living expenses to a minimum.
  - Reduce spending for clothing, recreation, entertainment, or other nonessential items.
  - Reduce energy consumption.
  - Postpone major purchases.
- Obtain help from a consumer credit counseling service in preparing a realistic budget and repayment plan.

Budget Worksheet

	← APPLICANT: *COMPLETE THIS AREA ONLY* →			TO BE COMPLETED BY INTERVIEWER	
	EXPENSES	WEEKLY	MONTHLY	ADJUSTED TO WEEKLY	ADJUSTED TO MONTHLY
HOUSING	RENT OR PAYMENT				
	ELECTRICITY				
	TELEPHONE				
	HEATING				
	TAXES				
	WATER				
	SANITATION				
FOOD	FOOD				
	MILK BILL				
	HOUSEHOLD GOODS				
CAR	GAS & OIL				
	REPAIRS, TIRES, ETC				
	LICENSE				
INSURANCE	HOSPITAL				
	CAR				
	HOUSEHOLD				
	ALL LIFE				
MEDICAL	DOCTOR				
	DENTIST				
	DRUGS				
CLOTHING	FAMILY				
	CLEANING AND LAUNDRY				
EMPLOYMENT	DUES - UNION & OTHER				
	SOCIAL SECURITY				
	INCOME TAX				
	OTHER				
	CHILD CARE				
PERSONAL	TUITION				
	BOOKS, PAPERS, MAGAZINES				
	BARBER & BEAUTY SHOP				
	ALLOWANCES				
	TOILETRIES				
	CIGARETTES & TOBACCO				
DONATIONS	CHURCH				
	ALL OTHER				
GIFTS	BIRTHDAYS				
	CHRISTMAS				
	ALL OTHER				
ENTERTAINMENT	MOVIES & PLAYS				
	DINNERS OUT				
	PARTIES				
	CLUBS & SPORTS				
	BEVERAGES				
	VACATIONS				
	BABY SITTER				
SAVINGS	SAVINGS BONDS				
	CREDIT UNION				
	BANK				
	OTHER				
MISCL	ALIMONY OR SUPPORT PAYMENTS				
	TRANSPORTATION (BUS, PARKING)				
	TOTALS ►	$	$	$	$

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Role Play Cards

Consumer 1
The January statement has arrived in the mail from the department store where you did most of your holiday shopping. Because your bills this month are higher than usual, you are unable to pay the "minimum amount" now due. You've paid your bills on time in the past.

Creditor 1
You handle the collections of debts owed by credit cardholders of a large department store. Credit customers are responsible for a majority of the store's December business. Generally you will work with customers who have temporary bill-paying problems.

Consumer 2
You purchased a television console from a small electronics retail store, putting one-third down on the $900 purchase price. The remainder will be paid in six $100 payments plus interest. However, you became ill and are now hospitalized. Reduced earnings and unexpected medical bills have made it impossible for you to make the required payment on the television set. You've already missed three payments.

Creditor 2
You are _____ of _____'s Elec-
(your name) (your name)
tronics Store. You lend money to creditworthy individuals to purchase electronic equipment. If one of your customers gets behind in making payments, you try to help by renegotiating payment terms. If it appears the problem is not temporary, you will repossess or encourage the debtor to voluntarily surrender the goods.

Consumer 3
Last winter you went on vacation in Hawaii. You "charged" most of your travel expenses through a local travel agency. If you paid within 90 days, you would incur no finance charges. The travel agency sent you its first bill after 90 days, but you could not pay. A second bill— including a finance charge—was sent a month later and indicated your account was "past due." You plan to pay the travel agency next month.

Creditor 3
You own _____'s Travel Agency and help
(your name)
many local residents plan and finance vacations during the year. You know it's difficult for some people to pay cash for their vacations, so you allow customers to "charge" travel expenses. If they pay within 90 days, there is no finance charge. Generally, no action is taken if a consumer fails to respond to your first bill. However, if no payment is made after you send a second bill, you turn the account over to a debt collector. You tell the debt collector to collect as much money as he/she can to reduce your loss.

Debt Collector 3
You are hired by _____'s Travel Agency
(Creditor 3's name)
to "collect" _____'s debt. Because
(Consumer 3's name)
Consumer 3 is not your customer, your primary objective is to obtain payment, not the consumer's future business. You use every means you can think of, including harassing and threatening the consumer, to collect the debt.

Role Play Observation Sheet

Role Play No. _____

Briefly describe situation:

_____

_____

_____

What did the consumer do to solve his/her bill-paying problem?

_____

_____

_____

Was the creditor able or willing to help the consumer? If so, how did the creditor help the consumer solve his/her bill-paying problem?

_____

_____

_____

What incentives did the creditor have to negotiate with the consumer?
What incentives did the consumer have to pay?

_____

_____

_____

Role Play Follow-up Sheet

Role Play 1

Consumer 1

Notify the department store as soon as you realize you cannot repay as agreed (before you receive the bill, if possible). Indicate to the creditor the reason for your bill-paying problem, your intention to repay, and when the creditor can expect repayment. Do not make additional credit purchases there or elsewhere until your payments are up to date.

Creditor 1

If the consumer notifies you of a bill-paying problem, you may want to consider renegotiating payment terms. If the problem seems to be temporary and if the customer has paid previous bills on time, eventual payment is likely. By accepting a smaller or later payment you will be helping your customer and at the same time maintaining his/her goodwill. Since the borrower is paying you interest on the credit, your loss will probably be minimal as long as you are paid.

Role Play 2

Consumer 2

If you think you cannot repay the creditor within six months, you may want to see if you can postpone payments until you are well. If you are not allowed to do this, you may want to surrender the television console voluntarily in order to meet your obligation to the creditor.

Creditor 2

To avoid losing the sale, you may want to consider accepting smaller payments or postponing payments until the debtor is well. If you cannot do this because of the uncertainty of when he/she will be able to return to work and resume making payments, you can either ask for the voluntary surrender of the television console or repossess it. You may then resell the television as used merchandise and offset most of your costs.

Role Play 3

Consumer 3

You probably should not have taken the vacation if you couldn't afford to pay the travel agency as agreed. At this time, you should notify the travel agency of your bill-paying problem and your intent to repay. See if the creditor will renegotiate the payment terms so you can pay later or make payments over a certain period of time. If the travel agency will not renegotiate, you must reduce your living expenses or prepare a debt repayment schedule which you can follow.

Creditor 3

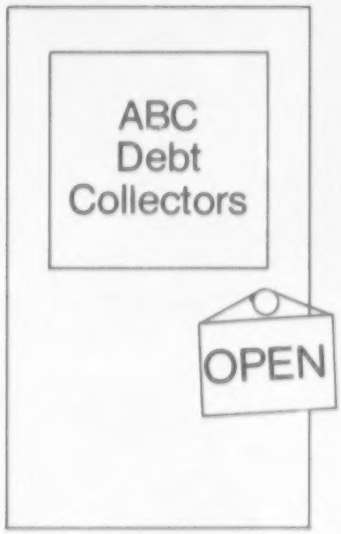
If the debtor has not notified you of his/her bill-paying problem and you do not know whether he/she intends to repay or when payment will be made, you may have to start debt collection activity. In your case this means turning the account over to a debt collector. Since you cannot recover any goods, you may want to renegotiate payment terms if the debtor appears willing and able to repay. Or, you may want to tell the debt collector to try to collect as much money as possible to reduce your loss.

Debt Collector 3

You may be violating the Fair Debt Collection Practices Act and be subject to legal penalties if you harass, abuse, or otherwise treat a consumer unfairly, e.g., call repeatedly at unusual times or places, or make unfounded threats. You may threaten the debtor only with consequences that you or the creditor usually take, and intend to take in this situation, if payment is not received. If having a good public image is important to the creditor, you may lose the creditor as a customer if you treat the consumer unfairly or with abuse.

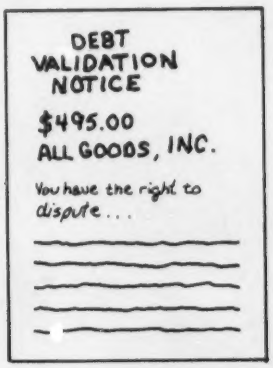
Your Fair Debt Collection Practices Rights

The Fair Debt Collection Practices Act protects consumers from debt collectors who engage in abusive, deceptive, or unfair practices.



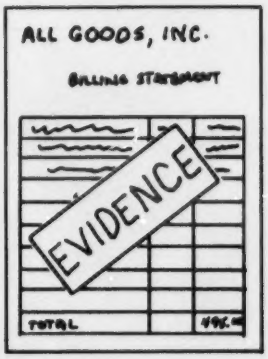
The Act only applies to third-party debt collectors. A person must abide by the law if he/she is in the business of collecting debts owed to a creditor. Creditors who collect their own debts are not covered by the Act.*

*Creditors who use a different name to give the impression that the account has been turned over to a debt collector must comply with the Fair Debt Collection Practices Act.

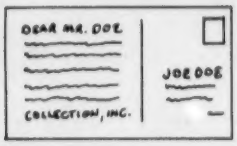


If you are contacted by a debt collector, the debt collector must send a written notice informing you of:

- the amount of the debt,
- the name of the creditor, and
- your right to dispute the debt and an explanation of what will happen if you do.



If you dispute the debt, the debt collector must provide you with written evidence of the debt before he/she can try to collect it.

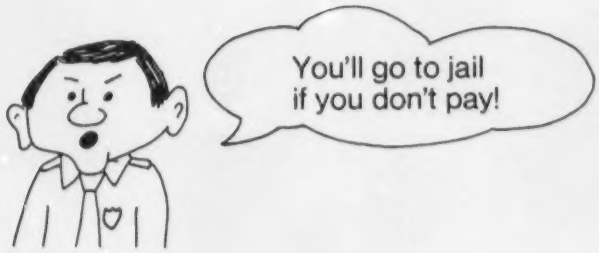


A debt collector who is trying to find a debtor cannot:

- tell another person that he/she is a debt collector unless asked.
- use a post card or indicate on the envelope that he/she is engaged in debt collection.
- contact a person other than the debtor more than once to learn the debtor's location.

A debt collector cannot:

- contact you at an unusual time (generally between 9 p.m. and 8 a.m.).
- make continuous or anonymous phone calls with the intent to harass you.
- contact you at your place of work if the employer forbids communication during working hours.
- use profanity or other abusive language.
- threaten to use violence or other criminal means to harm your person, reputation, or property.



A debt collector cannot:

- impersonate a police officer or government official.
- misrepresent the legal status of a debt.
- threaten imprisonment or other action which legally the debt collector or creditor could not take.
- make other false and misleading statements.

You can write to the debt collector saying you refuse to pay or that you want him/her to cease communications. The debt collector must stop contacting you except to advise you of any legal action he/she or the creditor intends to take.

If a debt collector violates the law, you may:

- notify the Federal Trade Commission, which supervises the debt collector.
- sue for actual damages and punitive damages up to $1,000 (including attorney's fees and costs).*

*Up to $1,000 in an individual action, or the lesser of $500,000 or 1% of the creditor's net worth in a class action.

Student Excercise 1

Directions: Decide whether the debt collection activities described below are legal or illegal, or whether the legality cannot be determined on the basis of the information given. Circle your answers.

1. A debt collector uses a post card to notify a consumer about a debt.

   legal illegal cannot be determined

2. A creditor telephones a customer at work and tells the person who answers the phone the name of his company.

   legal illegal cannot be determined

3. An employee of Northland Bank calls one of the bank's customers at 11:00 p.m. about late payments.

   legal illegal cannot be determined

4. A debt collection agency telephones a consumer about a debt at 11:00 p.m.

   legal illegal cannot be determined

5. ABC Stores, using the name ABC Collections, Inc., telephones a delinquent customer at 6:00 a.m.

   legal illegal cannot be determined

6. A department store's collection division calls a customer repeatedly during a 12-hour period.

   legal illegal cannot be determined

7. A credit union calls a member at his place of employment about a late payment.

   legal illegal cannot be determined

8. A debt collection agency telephones a consumer at work even though that person's employer does not allow personal calls.

   legal illegal cannot be determined

9. A person who collects debts for others threatens to "throw a consumer in jail" who refuses to pay.

   legal illegal cannot be determined

10. A debt collector hired by a furniture store tells a consumer that furniture purchased on credit will be repossessed if payment is not received.

    legal illegal cannot be determined

Freedom to Do Business . . .
Freedom from Abuse

Debt Collector's Right to Collect a Valid Debt

Consumer's Right Not to Be Harassed or Abused

Under the Fair Debt Collection Practices Act . . .

- A consumer cannot be contacted at an inconvenient time or place.
- A consumer's physical well-being, reputation, or property cannot be threatened.
- A debt or the consequences of not paying cannot be falsely represented.
- A debt is considered valid if a consumer does not dispute it within 30 days after receiving validation of the debt.
- A disputed debt must be verified before a consumer may be contacted again by the debt collector.

Case Study

Case 1

Karen Johnson receives a phone call at 8:00 p.m. from a person who identifies himself as a debt collector for ABC Collections, Inc. "I've had a difficult time locating you, Ms. Johnson," he says. "I'm calling you about the money you owe Fineline Furniture Company. You must pay, or we will be forced to take strong action against you."

Karen objects, stating she has never purchased anything from Fineline Furniture. The caller responds, "That's what they all say."

1. What is the debt collector required by law to do at this point?

2. What action must Ms. Johnson take to protect her rights under the Fair Debt Collection Practices Act?

3. What can Ms. Johnson do if ABC Collections, Inc., continues to call her about the debt before it is verified?

Case 2

John Kilpatrick has been out of work now for several months. His savings depleted, he can no longer make payments on his automobile loan. Since his account was turned over to a debt collection agency, it isn't uncommon for John to receive calls from the agency two or three times a day. John must answer his phone, since it may be a call about a job he applied for recently. John does owe the money, but he is unable to pay right now and wishes the phone calls would stop.

1. Can John do anything about the annoying phone calls from the collection agency?

2. True or False? If a consumer requests communications to cease, a debt collector can take no further action to try to obtain payment. Explain.

What If a Debt Collector Calls?

You receive a phone call from a debt collector . . .
Within five days, the debt collector must send you a written notice stating the amount owed, the creditor's name, and your right to dispute the debt.*
You dispute the debt.
You do not dispute the debt.
Within 30 days, you write to the debt collector and request verification of the debt.
The debt collector does not verify the debt.
You can insist that communications about the debt cease.
You receive verification of the debt or a copy of the judgment against you.
Communications about the debt may continue.
You notify the debt collector in writing that you refuse to pay and/or want communications to cease.
Debt collector must cease communications with you except to tell you what action if any he/she or the creditor will take.
You pay the debt being collected, or renegotiate payment terms with the creditor.

*See Topic 4, Transparency 4, this section.

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Debt Validation Notice

Creditor: Fineline Furniture Company

Amount: $1,599.98

Unless you notify us within 30 days after receiving this notice that you dispute the validity of the debt or any portion thereof, we will assume the debt is valid.

If you request verification in writing within 30 days, we will:

Obtain verification of the debt, or obtain a copy of the judgment, and mail you a copy.

Provide you with the name and address of the original creditor, if different from the current creditor.

ABC Collections, Inc.

Consumer Clout

I've always paid my bills on time . . .

I'm sure I'll find another job . . .

If you don't help me, I'm going to warn all my friends about you . . .

I won't buy another thing from from you . . .

He's a good customer and has paid on time before . . .

We want to help . . . and minimize our losses.

He told us about the problem . . .he intends to repay.

We could always repossess the merchandise . . .

1. What do you think the creditor might do in this situation?

2. What might be the consequences to the creditor of not "negotiating" with the consumer?

3. If three months later the consumer still hasn't paid, what action(s) might the creditor take to obtain payment or reduce losses?

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It Doesn't Pay*

MR. KELLY: Most everybody I deal with wants to pay their bills. They've just got themselves in a bind, whether I'm working with a business or a consumer. I do work for many major banks when they have problem loans. Most of these people want to do everything they can to get out of debt. When you talk about the crooks, you're talking about just a very, very small minority. Successful collection is a matter of being able to help people work their way out of debt in some way. It's not a matter of going in and yelling at people when they're broke. That doesn't do you a bit of good. If they're down and out, what are you going to accomplish by yelling at them or by calling their employer or calling their wife? What you want to do is get the guy back working and have him regain his feeling of self worth. You've just got to be sure you've got a little rope tied around his legs so when he starts making money again you can say, "Hey, remember me? I helped you out."

If a guy's business is going bad and going down the drain, the bank is going to lose a ton if he goes under. The thing to do is help him build himself back up, get him going again, get management in there and get somebody to help him. Don't beat him over the head. That's not going to do anybody any good and this happens all the time.

SENATOR RIEGLE: You have been in this business quite a long time. And your testimony is that these high pressure tactics—the intimidation, the phone calls in the middle of the night, the phony legal documents—that those tactics are just not necessary and, in your judgment, are not even sound from a business point of view because there are better ways to get the job done?

MR. KELLY: Well, they're stupid. It's stupid to go after somebody in an animal-like fashion to collect a bill. Why not go in and make friends with him and sell him on the idea of paying? That way you're going to end up on the top of the pile, underneath the mortgage and the car payment, instead of thrown over in the wastebasket because he hates you because you have been calling his wife and kids and things like that.

*U.S. Congress, Senate, Subcommittee on Consumer Affairs of the Committee on Banking, Housing, and Urban Affairs, *Fair Debt Collection Practices Act: Hearings on S. 656, S. 918, S. 1130, and H.R. 5294*, 95th Cong. 1st sess., 13 May 1977, pp. 198-99.

Student Exercise 2

Directions: Decide whether the consumer, debt collector, or creditor bears the costs described below of the Fair Debt Collection Practices Act. Circle your answers.

1. A debt collector raises his collection fees when it takes longer to collect debts.

   consumer debt collector creditor

2. A creditor decides to impose stricter standards for granting credit in response to the higher costs of debt collection.

   consumer debt collector creditor

3. A creditor raises the interest rate charged on new loans to cover the higher price of debt collection.

   consumer debt collector creditor

4. A consumer pays for legal advice to find out whether or not action threatened by a debt collector can legally be taken.

   consumer debt collector creditor

5. Due to the increased costs of using debt collection services, a creditor decides to collect her own debts.

   consumer debt collector creditor

6. A consumer spends 30 minutes writing a letter to a debt collector requesting communications to cease regarding an unpaid bill.

   consumer debt collector creditor

7. A debt collector sends a debt validation notice to a consumer who has been notified about the debt.

   consumer debt collector creditor

8. Because the costs of debt collection have increased, a creditor provides less credit to his customers.

   consumer debt collector creditor

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